UNITED STATES BANKRUPTCY COURT

SOUTHERN DISTRICT OF NEW YORK

Case No. 18-23538-rdd

- x

In the Matter of:

SEARS HOLDINGS CORPORATION,

Debtor.

- x

United States Bankruptcy Court

300 Quarropas Street, Room 248

White Plains, NY 10601

October 7, 2019

1:07 PM

B E F O R E :

HON ROBERT D. DRAIN

U.S. BANKRUPTCY JUDGE

ECRO: NAROTAM RAI

HEARING re Notice of Hearing : Notice of Continuation of Hearing on Confirmation of Modified Second Amended Joint Chapter 11 Plan of Sears Holdings Corporation and Its Affiliated Debtors

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P R O C E E D I N G S

THE COURT: Okay. Good afternoon. In Re: Sears Holdings Corporation, et al.

MR. SINGH: Good afternoon, Your Honor. Sunny Singh, Weil Gotshal, on behalf of the Debtors.

Your Honor, we're here for the continued confirmation hearing. Before we pick up with where we left off, I thought I could give the Court with some updates. We do have at least one resolution I'd like to announce, as well as some other matters.

THE COURT: Okay.

MR. SINGH: So, Your Honor, following the hearing last week, I would like to report that we have settled the objection filed by Pearl Global Industries, with Mr. Wander, who is here. I'm just going to recite the terms of the parties' agreement and I'll ask him to just confirm.

Your Honor, Pearl Global Industries will receive an allowed claim of $1,130,000 without offset or deduction. That's an administrative expense claim. That's reduced, Your Honor, from something in excess of $1.5 million that had been asserted.

There will be a waiver, by the estate, of any potential preference claims against Pearl. An additional $1 million, Your Honor, will be contributed from the carveout to the estate for distribution in the initial distribution.

So, Your Honor, under the consent program we had the initial distribution of $20 million, so now that will be $21 million and it will include this additional increment of $1 million from the carveout.

THE COURT: Okay.

MR. SINGH: In addition, Pearl agrees, excuse me, that it will opt-in to the consent program and that it now withdraws its objection and supports confirmation of the plan.

Your Honor, those are the terms with Mr. Wander. Maybe I'll just ask him to confirm in case I missed anything or --

MR. WANDER: That's correct, Your Honor.

THE COURT: Okay. Was --

MR. SINGH: So, Your Honor, that issue is resolved. I would just like --

THE COURT: Was the assessment of Pearl's claim and preference risk done on an assessment of the merits?

MR. SINGH: Yes, Your Honor. So as I mentioned, Mr. Wander's client, Pearl, had asserted a claim of an administrative expense at -- in excess of $1.5 million. So over the weekend, and finally last hearing, we considered, you know, the validity of his claims. He had -- you know, they had somewhat of a world import issue, also inducement arguments with respect to 503(b)(1), which were sort of

legal disputes between us and we think we've resolved those at a fair place.

We also did look at, obviously, the preference exposure, you know, that has -- that Pearl had, took that into consideration, as well as the incremental $1 million coming in from the carveout. And, Your Honor, we did review all of that with the Creditors Committee, Akin Gump, in particular and, you know, everybody's signed off and on board as to where those issues have now landed.

THE COURT: Okay. And did -- was that preference resolution consistent with the analysis by the firms that had been retained to do the --

MR. SINGH: Yes, they were -- we were coordinating with them every step of the way, and it took into account, sort of, you know, what potential defenses could be asserted, and at the end of the day what we thought the exposure really could be. So yes, we -- you know, that was in complete coordination with the ASK firm.

THE COURT: Okay.

MR. SINGH: So, Your Honor, we think we've landed in a good spot there. Just one or two other changes I would just like to note, with respect to the consent program. Your Honor, following the hearing last week, and some of the concerns the Court raised with respect to those creditors, administrative expense creditors, who neither opt-in, nor

opt-out of the settlement, so that sort of third class we were talking about. So, Your Honor, we've changed the consent program so that those parties now, their aggregate recovery, instead of being capped at 75 cents of the allowed amount of their administrative expense claim, they would be capped at 80 percent of the allowed amount of their administrative expense claim.

So you've really got, sort of, three categories of administrative expense creditors. Those who affirmatively opt-in. And we've made the opt-in timing the same for both, so everybody gets 33 days to opt-in or opt-out. Those who affirmatively opt-in will get the benefit of the initial distribution, they will also get -- but they will be capped at 75 cents of the allowed amount of their claim. The second category, who neither opt-in nor opt-out, they will be bound by the administrative expense consent program but they will have their aggregate recovery capped at 80 cents. And although they won't participate in the initial distribution, the second distribution first has to go to true them up to the initial recovery. And then finally, anybody who opts-out, of course, will retain their rights under the plan to be paid in full, a hundred percent of the allowed amount of their claim on the later of the effective date or the date that the claim actually becomes allowed.

So we've made those changes and we did file a

proposed confirmation order that reflects those changes, Your Honor. We'll have some more clean up based upon what I announced earlier. And we also did file a revised form of notice that would go out, and Your Honor has a copy of those and we can review those towards the end, if Your Honor would like to.

But that basically takes into account some of the issues that you had raised and also just making it clear, we included a chart that sort of makes it clear, you know, what happens if you are in the opt-in category, what happens if you're in the opt-out, and what happens if you're, you know, in neither opt-in or opt-out. So hopefully that's much clearer. And we added, you know, some of the information from the declarations, in particular, about estate assets, et cetera.

THE COURT: And the risk factor discussion?

MR. SINGH: Right, exactly. We updated all of that.

And Judge, just a couple of other changes or issues we're working through. ESL and Cyrus had asked us to just make clear that the segregation of funds that we've been talking about in connection with the litigation trust funding, that's the $25 million and the 10 million, they are going to send us some language and we may just recite it in the record later, but I just wanted the Court to know that

we're talking through that to make it clear that it's not -- those assets, although they're being put in segregated accounts, they remain the property of the estate, they're not, sort of, being removed as you would think of maybe carveout funds that go to a trust fund, but they're sort of available --

THE COURT: That's consistent with the language you've already offered up that --

MR. SINGH: Correct. Paragraph --

THE COURT: -- distribution into the trust doesn't --

MR. SINGH: Exactly. It's Paragraph 59 of the proposed confirmation order.

THE COURT: Okay.

MR. SINGH: And then I think Cyrus had requested additional notice, which we've agreed to. Just 20 days, we would provide notice. So we put in, you know, the sort of reporting prior to the effective date, we would also add in, you know, prior to make any post-effective date distributions, we'll provide parties-in-interest with 20 days' notice so they have an opportunity to know that.

THE COURT: Just the first distribution?

MR. SINGH: Just -- well, any distribution following the effective date.

THE COURT: Oh, okay.

MR. SINGH: Yeah.

THE COURT: All right.

MR. SINGH: So, Your Honor, those are some of the changes we're working through, I just wanted to give the Court an update before we started with the balance of the hearing. But I'm happy to proceed however you'd like at this point.

THE COURT: All right. Well, I've seen those documents, I also saw the proposed fourth supplement that has the proposed terms for the --

MR. SINGH: Oh, yes, I failed to mention --

THE COURT: -- liquidation trustee's --

MR. SINGH: Yes. We did file --

THE COURT: -- compensation?

MR. SINGH: Exactly. I failed to mention. I apologize.

We did file the proposed compensation for the litigation trustees. That would kick in, Your Honor, should you enter the confirmation order, basically on the confirmation date, because those individuals are stepping in as litigation designees, you know, as soon as the confirmation order is entered, other than with respect to the preference claims, because that's outside of their mandate. But then post-effective date it, sort of, would include the preference claims. But we did file that,

parties have three weeks to object. We have extra copies if anybody didn't see it. We filed it just this morning before the hearing. And so that is now always been on file, and we took it out of the confirmation order.

THE COURT: Okay.

MR. SINGH: Okay. Thank you, Your Honor.

THE COURT: Okay. So I think where we left off Mr. Fox was speaking. And I have to say, at the end of a very long hearing, I think I did a disservice to Mr. Fox. He's always been a very aggressive advocate, but never untethered from reality. And I hope he didn't have an existential moments over the weekend where he doubted that, but in any event, if you did, I'm sorry if you did.

MR. FOX: Actually, Your Honor, I thought you handed me the keys. Thank you.

THE COURT: Well, then maybe you did.

MR. FOX: Thank you, Your Honor. I appreciate that. It was a long day.

I do want to just make a couple of preliminary comments before I get back to the argument. One, I want to be clear, Wilmington Trust is the indentured trustee for the 6-and-5/8th percent senior secured notes to 2010. That's the capacity in which I appear today, not on behalf of anybody else.

And just so it's clear, in case there's any

confusion, ESL does not own any of how to notes. And -- so I'll leave it at that.

Secondly, Your Honor, just as a preliminary matter, as they say in public speaking, tell them what you're going to say, say it, and then then tell them what you said. So I started into the argument about the settlement, but I want to be clear, and I'm going to say this at the end, that there is a plan here that Your Honor could confirm, assuming that the other issues that have been raised by others are addressed, that does not require the plan settlement to be approved. And in fact, the very fact that that plan exists I think may make it impossible for the Court to approve the plan settlement, but I'll come to that a little bit later.

To get back to it, Your Honor, the -- in making a determination as to whether the facts the Debtors have elicited satisfy the requirements to confirm the -- or to approve the planned settlement, the Court must also look to the Debtors' action in this case, not just to the declarations that have been offered into evidence. And we've included, in the exhibits, the documentation that shows those actions.

In particular, Your Honor, on February 9th, 2019, the Debtors announced a settlement with the PBGC that -- to allow the PBGC an $80 million priority claim and an $800

million unsecured claim. Notably, that agreement provided that the Debtors would not seek to substantively consolidate the Debtors' estates. Following that, on April 17th, 2019, the Debtors filed a plan, which again, did not provide for substantive consolidation of these cases. It wasn't until May 16th, a month later, that the Debtors filed an amended plan which purported to settle substantive consolidation by substantively consolidating the Debtors.

And according to the confirmation brief, pursuant to the plan settlement, the PBGC agreed to settle substantive consolidation issues under the plan, that's at Paragraph 261 of Docket 5144. So it seems, at least in the initial go round, or the initial rollout of the substantive consolidation settlement, it was allegedly a settlement between the Debtors and the PBGC over an issue that was not in dispute between them since they had both agreed not to do that and the Debtor had filed a plan that provided that it would not do that.

So a debtor can settle or compromise a -- you know, can enter into settlements and compromises, but the definition of settlement or compromise requires that there be an active dispute. So at least at that time, with respect to the PBGC, there was not.

So -- and when we asked Mr. Murphy, and your comment -- your request before the lunch break on Thursday

was that we provide you with the specific areas of testimony that we had designated from the deposition, so I'll do that as I go through, but Mr. Murphy didn't know what dispute the Debtors referred to in the disclosure statement for the amended plan either.

When he was asked about that, this is on Page 72, Line 11 of the deposition testimony that was designated, the question was: "So it says discuss below, after filing the initial plan and disclosure statement on April 17th, 2019, the Debtors and the PBGC agreed to certain modifications to the PBGC settlement in exchange for the settlement of disputes and potential litigation regarding whether the Debtors should be substantively consolidated. Do you know what disputes this is referring to?" Answer: "Specifically, I was relying on counsel for the detailed disputes. At a high level it's their claim for substantial unsecured debt and administrative debt claims." Question: "Whose claims?" Answer: "The PBGC." Question: "Well, it refers to a settlement of disputes and potential litigation regarding whether the Debtor should be substantive consolidated. So who are the parties to that dispute; do you know?" Answer: "I'd have to rely on counsel for that specific answer." Question: "So you don't know what dispute and you don't know who the parties were; is that correct?" Answer: "I'm not sure what specifically. This says settlement of

disputes and potential litigation, and I'm taking it at face value. There were disputes and litigation. I'm not -- I'm providing financial information analysis -- and analysis with regards to any settlement offers."

Mr. Genender: "To be fair, he's just asking if you know who the parties to this -- to the dispute referenced understand that language are." Mr. Fox: "That's correct." Mr. Genender: "If you don't know, he's asked -- answer I don't know."

Mr. Murphy didn't know why the Debtors decided to file a substantive consolidation plan on May 16th, 2019 either and he was involved in that decision. Again, he was asked -- I asked him: "Between April 17th, 2019 and May 16, 2019, what changed that led to the Debtors to file a substantive consolidation plan rather than the nonconsolidation plan filed on April 17th? What changed in that one-month period?" Answer: "I can't answer." Mr. Genender: "To be fair, he asked you to rephrase it, you repeated it. Just to be fair, he asked you to rephrase it." By Mr. Fox: "Do you understand my question, Mr. Murphy?" Answer: "Yes." Question: "Is there some reason why you can't answer it?" Answer: "Basically I wasn't involved in the high-level discussions regarding that final decision."

He then went on, though, to provide that it appears that the real problem was the administrative

insolvency of Debtors other than Kmart. So I asked him: "So far as you know, is it fair to say -- is it fair to say, as far as you know, sitting here today, nothing changed between April 17th, 2019 and May 16, 2019 that caused the Debtors to switch from a nonconsolidation plan to substantive consolidation plan?" Mr. Genender: "I'm going to object. That misstates his testimony and lack of foundation." Answer: "I'd have to reflect on that period of time and what I have in my declaration to see if there's a better answer than say other than during that 30 days there was additional analysis and discussions. It's an evolving process. That's as far as I could go."

Question: "What additional analysis are you referring to?" Answer: "The intercompany analysis, the waterfall effect of where a value is landing with regards to each Debtor." Question: "When you say the analysis of where value is landing, how is that relevant to the analysis of whether you find -- filed a substantive consolidation plan or not?" Answer: "Based on the information and the analysis of the intercompany waterfall. If you looked at the deconsolidation liquidation analysis, the value at the end of the waterfall was substantially ending up in the Kmart corporation entity." Question: "So is it fair to say that the problem became that there were a bunch of administratively insolvent Debtors on a standalone basis,

after you did your analysis, and maybe Kmart and some others that were administratively solvent?" Mr. Genender: "Objection to form." Answer: "Hypothetically, based on that analysis, yes."

Despite the fact that Mr. Murphy was not involved in the decision to change to a substantive consolidation plan, although he's their witness on this, and the real problem was administrative solvency of some Debtors, the Debtors used Mr. Murphy to try to justify substantive consolidation. Mr. Murphy enumerates what he says are other factors for substantive consolidation, and that's at Paragraph 24 of his declaration.

But when I asked him if he knew what the factors for substantive consolidation were, he couldn't answer and he said he's not a lawyer. The question was: "How do you know what the factors are for consolidation?" Mr. Genender: "He answered questions about the facts." Mr. Fox: "I'm not asking that." Question: "You can answer." Answer: "Please rephrase the question. I just don't want to make a legal -- I'm not a lawyer, so I'm not going to answer a legal question."

Mr. Murphy asserts, in his declaration, that Creditors dealt with Debtors on a consolidated basis. And that's one of the two prongs in the Augie/Restivo Test, as you know, to determine whether or not substantive

consolidation is appropriate. But he really has no basis for his assertion. First of all, the loans specifically indicate who the borrowers and the guarantors are.

The question, this is at Page 126 of his deposition: "When you say the creditors, and you refer to the lenders, particularly dealt with Sears as a consolidated company, isn't it the case that all the loans specifically indicate who the borrower is, or who the guarantors are of those loans?" Mr. Genender: "Objection. Form." Answer: "Yes."

And the trade creditors had written contractors, but Mr. Murphy never even looked at them, he just determined that they must have been confused. On Page 72 of the deposition, Question: "Mr. Murphy, take a look at Page 13 of your declaration that's been marked as Exhibit 6, if you would." Answer: "Okay." Question: "In Paragraph 24, at the bottom of that page, you say, at the second sentence of subparagraph A, 'Many Creditors conducted business primarily with three Debtors, Sears Holding, Sears Roebuck and Kmart Corporation.' Do you see that?" Answer: "Yes." Question: "Then you say, at the bottom of that paragraph, 'Sears Roebuck purchased a significant amount of the store merchandise, both in sold Sears and Kmart stores, right?" Answer: "Yes."

Question: "When the Debtor entered into their

transactions that are referenced here with whichever Creditor, and I'm not talking about loans now, I'm just talking about trade, were there written contracts, or purchase orders, or invoices pursuant to which those goods and services were purchased?" Answer: "Yes." Question: "Okay. And did those invoices, or contracts or purchase orders list the name of the Debtor which was buying the goods or services?" Answer: "Yeah, I don't know." Question: "You don't know?" Answer: "For specific invoices for that the Debtors specifically did I didn't get into that detail." Question: "Never looked at that?" Answer: "No, not for this, no." Question: "Not for any part of your substantive consolidation analysis?" Answer: "No."

Now, we did take a look, just randomly, at a couple of proofs of claim that are on the docket and in fact the proofs of claim have attached to them specific invoices which specifically have the legal name of the legal entity that purchased them. We included four of them, it's Joint Exhibit 57, 58, 59 and 60, which specifically indicate who those entities are dealing with.

And then what we did was we found entities where the same entity filed different proofs of claim against different entities, because they had different claim -- they had different contracts that specifically name those

different entities. So what appears to be to be the case is the Debtor made an assumption about this, or Mr. Murphy did, but never actually looked and in fact the evidence would seem to suggest otherwise.

Mr. Murphy also indicated, though, that the financing method that the Debtors were using was not unusual for a large public company. Page 174 of his declaration, I asked him -- I said, "Now turn to Page 14, if you would of Exhibit 6, at the bottom of the page in Paragraph F. Do you see that?" Answer: "Yes." Question: "So it says there, 'Financing was provided principally through Sears Holdings or Sears Roebuck Acceptance Corp with the majority of the remaining Debtors providing guarantees of the debt. Funds were centralized and available for all entities.' Do you see that?" Answer: "Yes." Question: "Okay. Is this unusual in terms of the large public company operation that has outstanding loans? Is this description unusual?" Answer: "Not in my experience."

Now, Mr. Murphy says, in his declaration in Paragraph 24, at Pages 14 to 15, there are a number of factors which are satisfied to show that there may have been confusion among the Creditors as to what entities they were dealing with, and it's the usual list of overlapping board members, a central office, centralized operations, et cetera, you know, tax statements, consolidated financial

statements being filed, all those things. First of all, with respect to tax returns, they're required to file consolidated tax returns and they're required, by SEC rules, a public company is, to file consolidated financial statements.

But the problem with all this is that, among other things, the Debtors knew all of this when they got the PBGC deal which was in early 2019. It was just figured out after filing the plan in April, or even after agreeing in February who the directors were of which entities, where the offices were located, which is in Huffman Estates, as the world knows, or, you know, that they had centralized financial reporting, Treasury, HR, Tax Planning, Real Estate Management, Internal Audit, et cetera. All of that was known, that was no secret to anybody. So nothing changed between the time that the Debtors filed their -- at least with respect to this prong of substantive consolidation, with respect to the issue of Creditors not understanding who they were dealing with.

And I think it's also important to note that this was a public company that filed financial statements, and you can take judicial notice of those, the fact that it was very clear to everybody, or anybody who bothered to look, that they had outstanding loans, that those loans were guaranteed at multiple entities within the Debtors. The

documents are actually in the SEC files. That they had multiple, you know, obligations of each of the entities to the PBGC as part of the control group. This wasn't any surprise to anybody, or certain not to other -- to trade creditors or others who dealt with a single entity, when they decided to enter into agreements, or make loans, or sell goods and services to any of these debtor entities.

Now, with respect to the analysis of hopeless entanglement, Mr. Murphy, and I think you've heard this now, testified that he joined M3 in December of 2018, which was three months after the bankruptcy cases were commenced, but perhaps more importantly, he hasn't done this type of an analysis before. When I asked him, at Page 40 of his declaration, "Have you done this sort of analysis at other companies besides the Sears Debtors?" Mr. Genender: "Objection." Answer: "I would say there are very few people who've done this type of analysis. There are a few, very few companies the size of Sears with the methodology they used for using intercompany accounting to track all their activities, certainly not the size of the company. This is -- I've done second intercompany analyses for other liquidation analyses for other companies, never the size of this one." And then at Page 41, Question: "All right. Let me ask it this way. Have you ever performed a similar analysis of intercompany claims at a company the size of

Sears, laying aside the volume of transactions?" Answer: "No."

Now, Mr. Murphy claims that there were potential difficulties in reviewing financial records --

THE COURT: I'm not sure what that question --

MR. FOX: I'm sorry?

THE COURT: That question didn't seem to make any sense to me. I mean, is there any such entity?

MR. FOX: There may be.

THE COURT: It would seem to be almost inconceivable that there'd be a company like Sears that wouldn't have the same types of intercompany transactions --

MR. FOX: Well --

THE COURT: -- because Sears has these three main operating centers. But anyway, you can go ahead.

MR. FOX: Mr. Murphy claimed a potential difficulty in reviewing the financial records and in fact that was not actually the case. When Mr. Murphy looked at post-petition financials, and found what appeared to be incorrect entries, it turned out that Sears could show him where those entries had been corrected.

So at Page 31 he testified, Question: "So those adjustments that you concluded Sears had entered incorrectly during the post-petition period?" Answer: "Those were adjustments when we queried, we followed up with the

company, that the company said, oh, that was incorrect, here's where we corrected it." Question: "And were their corrections accurate?" Answer: "They appeared accurate based on their responses. Again, as far as the intercompany activity was concerned, for the accountant perspective, if the debit and credits matched, and their explanation for what the correction was meant to be, then we moved forward. We made sure we either identified the correction in our overall matrix to make sure we weren't grossing up receivables and payables this far, or due to and due froms from a company sense for our net results." Question: "Well, what I'm trying to understand is did you find errors in work that Sears had done that were not corrected?" Answer: "No."

And Mr. Murphy's conclusion was that the activity was -- that the activity he summarized was consistent with the balance sheet. So on Page 39, when I asked, "Well, you said it was a process for you to understand how the intercompany transactions were recorded on the balance sheet and how the balance sheet damages would match up. So my question is, after you went through that process to understand this, what did you finally determine?" Mr. Genender: "The balance sheet changes, you said damages." Mr. Fox: "I'm sorry, changes." Mr. Genender: "Objection. Form." Answer: "Our conclusion was that the activity we

were summarizing by debtor entity for due to and due from, based on the methodology of the company the Debtors used to aggregate the various entries, was consistent with what was reported in the balance sheet."

Mr. Murphy's analysis left him with an 80 to 90 percent confidence level of the post-petition intercompany balances. And on Page 54 when I asked, "Now turning to Page 3 of Exhibit 1, you say that after you receive -- you reviewed analysis and discussions with Sears management, you have an 80 to 90 percent confidence level of a current intercompany post-petition activity as a reasonable indication of the due from and due to balances amongst the Debtors; is that correct?" Mr. Genender: "Objection. Form." Answer: "That's what I stated. Yes." Question: "And what's the due from and due to balances amongst the Debtors on just a post-petition basis, right?" I'm sorry, let me read that again. Question: "And that's the due from and due to balances amongst the Debtors on just a post-petition basis, right?" Answer: "Yes."

Now, Mr. Murphy complains, in his declaration, as did the Debtors in their disclosure statement from May, starting in May, which seems, in some cases, to word-for-word mirror what Mr. Murphy's declaration then said in September, but he refers to an antiquated system, but nevertheless basically admitted it does not affect the

company's accounting. It simply was problematic for him because he couldn't push a button and get a query of what all the intercompany transfers were, so that he could look at them and review the history.

Question, this is on Page 57, starting on Line 6: "Now, in the next point underneath that, as part of the second bullet point, it says 'Legacy accounting systems are not adequately robust in our view. What do you mean by that?" Answer: "They're not modern, they're antiquated and we weren't able to request a summary of intercompany transactions that made it easy to understand the activity between all entities." Question: "You were not able to obtain this for most petition activity?" Answer: "Correct."

Question: "Well, does the fact that the accounting system is what you call antiquated mean that it does not correctly keep track of the company's accounting?" Answer: "No, I'm not saying that." And he went on.

And on Page 56, Question: "But to go back to my question, does the fact that the accounting system is, as you call it, antiquated, mean that it was not properly handling the accounting for the Debtors?" Answer: "That's a conclusion for the auditors. For a consolidated financial statement, you have to talk to their auditors about that type of question. My point was more specifically to

intercompany transactions."

Question: "Well, because the accounting system is antiquated, are you saying that sometimes it added two plus two to equal five instead of four? Are you saying it was adding or subtracting incorrectly?" The Answer: "No."

On Page 6 he's continuing. Question: "And if you -- if this antiquated accounting system is not keeping proper track of the books and records, would you expect that the auditors would not be able to issue an opinion?" Mr. Genender: "Objection."

Question: "Of the annual audit." Mr. Genender: "Objection, form." Answer: "That's my understanding."

Question: "What's you understanding?" Answer: "For public accountants on a consolidated -- on a consolidated financial statement which they are opining on, they had to have comfort that the consolidated financial statements met their requirements as far as generally accepted accounting principles."

Question: "And you're not aware that the accounting statements did not meet the requirements, right?" Mr. Genender: "Objection, form." Answer: "If they provided clean opinions, then that would be an indication that they were okay for the consolidated financial statements."

Question on Page 62: "Are you aware that the company's outside auditors provided anything other than

clean opinions?" Mr. Genender: "Asked and answered (indiscernible)." Answer: "I don't know." Question: "I'm sorry." Answer: "I don't know."

Now, the other thing is that this all related to the post-petition activity, which is what Mr. Murphy was really looking at. Mr. Murphy didn't really analyze prepetition accounting activity.

When I asked him on Page 91 of his deposition transcript, Question: "You previously, as I understood your testimony, were talking about your analysis of post-petition intercompany transactions. Was there also an analysis that you conducted of prepetition intercompany activity?" Answer: "Yes."

Question: "Okay. And was that part of the same analysis you conducted with respect to the post-petition activity that we've already talked about, or was that a separate analysis?" Answer: "With regards to the prepetition analysis, there wasn't an organized effort similar to what we did with the post-petition detail."

The prepetition analysis was simply limited to responding to questions about what Mr. Murphy referred to as the due to/due from by Debtor, by which he means on the intercompany basis, which Debtors owed money to which other Debtors, and which Debtors were owed money by other Debtors.

And so when I asked him about that starting at

Page 93, Question: "You said in your prior answer that you responded to questions that came up. As I understood your prior answer, and I'm paraphrasing, it's my understanding that you were responding to questions that came up with respect to prepetition intercompany activity. My question is was your analysis of prepetition intercompany activity limited to responding to those questions that came up, or was it more expansive than that?" Mr. Genender: "Objection, form." Answer: "It was more to respond to questions based on our observations of the prepetition balances from looking at the balance sheet."

Question: "And what questions were those?" Answer: "Primarily questions regarding what type of effort would we need to perform in order to break out the prepetition balances so that we understood the due to/due forms by Debtor."

Question: "And did you prepare any kind of written analysis that would set forth that analysis?" Mr. Genender: "Objection, form." Question: "Or that effort?" Answer: "No."

Question: "And do you know when that analysis was undertaken?" Answer: "Which analysis?"

Question: "The one you're referring to of the questions that came up with respect to prepetition activity." Answer: "That occurred over the period from

January through the filing of this claim."

Question: "And that was May 16th?" Answer: "Yes."

Now, with respect to the inter -- in the disclosure statement, the -- and this is the May 16th, and it's pretty much the same since then, the Debtors have indicated the -- pointed to the fact that intercompany amounts were netted out.

When I asked Mr. Murphy about that, Question: "Let's see. Go to 11 -- go to 10 lines from the bottom of Page 53 -- and this -- that was of the May 16th version of the disclosure statement. And the sentence in the middle starts in the middle of the page, says while the Debtors' accounting systems identifies the entities to which intercompany payables are due or for which intercompany receivables are due in the ordinary course, the millions of entries are netted automatically by the accounting system and are not summarized by Debtor. Do you see that sentence?" Answer: "Yes."

Question: "Okay. Is that sentence accurate?" Answer: "Yes."

The point is that the Debtors did in fact keep track of their intercompany accounts, and they did in fact net them out. Typically what you'll find is that that's not the case.

Mr. Murphy didn't analyze or, I believe,

understand the interplay between the intercompany claims and the cash management system. If you look at the Debtors' schedules, they'll either show in Schedule AB intercompany obligations owed to a particular Debtor or in Schedule EF intercompany obligations owed by that Debtor entity. And in some cases, there are some Debtors that neither have a receivable -- an intercompany receivable or an intercompany payable.

What these ultimately are, to the extent they even have -- either have a receivable or payable is an obligation effectively to the centralized cash management system. And when I asked Mr. Murphy about that, this is at Page 99. I asked him: "When you say not settled, do you mean did not hand cash around to settle those; is that what you mean?" Answer: "In its simplest form. But the bottom line is that they did not either collect on the receivables or pay on the payable."

Question: "To each other?" Answer: "Correct."

Question: "But they kept track of how much each one owed to each other one, and they did, and they netted those out, right?" Mr. Genender: "Objection, form." Answer: "In the millions of transactions that relied on the balancing, the general ledger balancing effort by the, you know, the information systems, millions -- billions of transactions, that as long as those transactions netted to

zero on a consolidated basis, the company moved on to the next period. Where the difficulty arises is when you want to now separate the intercompany transactions from one big bucket that needs to net to zero to individual Debtors."

Question: "Well, if I owe you a dollar, and you owe Mr. Genender a dollar, and Mr. Genender owes me a dollar, are you saying that it's not appropriate for us to just agree that nobody owes anybody anything because we netted those transactions, or do we actually have to pass the dollar around to each of us to settle the transaction?" Mr. Genender: "Objection to form." Answer: "Under that example, if we all agreed to settle that way, then that would be the settlement. But if you owed me a dollar, in a one-dollar example, it's actually too simple. If you owed me a dollar but that dollar went to a bunch of other creditors and I have no money to pay Mr. Genender, then it's not fair. He's not going to receive any recovery from his payable or receivable from me."

Question: "Okay. But the Debtors' records reflect the fact that some Debtors are in the deficit position, correct?" Answer: "On a net basis, correct." Okay.

Question: "And they just simply don't have the ability to pay their creditors. That's what it means to be bankrupt, right?" Mr. Genender: "Objection, form." Answer: "You're going to have to rephrase that question as to how

I'm supposed to answer that with regards to intercompany."

Question: "Well, it's the case that on some of the schedules that the Debtors filed, some of them have intercompany receivables that are owed to them, and some of them have intercompany payables that they owe to other Debtors, and some of them have neither intercompany receivables nor intercompany payables, correct?" Answer: "I couldn't answer that because that analysis was not done."

Question: "Well, the Debtors filed schedules and statements under penalty of perjury that say exactly that. Are you saying those are not true?" Mr. Genender: "Objection, form. Argumentative. Come on." Answer: "The schedules were filed based on the best information the company had -- the Debtors had at that time, and those were net balances."

Question: "Right. Does that mean they're not accurate?" Answer: "That means that the detail didn't identify each individual Debtor."

The Debtor had a -- Question: "The Debtor had an integrated cash management system, correct?" Answer: "That's my understanding."

Question: "And all the cash from all the different Debtors float up into the integrated cash management system, correct?" "Again, my understanding."

Question: "Okay. So if Debtors put cash into that

system, or -- then they'd get a credit. And if they took cash out of that system on a net basis, they'd owe a payable, correct?" Answer: "Correct."

Question: "Okay. And effectively, aren't all those intercompany payables and receivables simply claims against the integrated cash management system and the funds that are available there?" Mr. Genender: "Objection, form." Answer: "You've got to rephrase that because I'm not sure what that question is for."

Question: "Do you not understand the question?" Answer: "No, I don't."

Question: "Okay. The Debtors kept books and records of intercompany activity, correct?" Answer: "Correct."

Question: "Okay. But the Debtors did not -- did not settle between themselves on a periodic basis by actually transferring cash or property, correct?" Answer: "Correct."

Question: "They simply kept track of their books of those transfers, correct?" Answer: "Correct."

Question: "Okay. To the extent that the Debtors were dealing with cash and they were running a retail business, so cash would come in every day, they sold product, all that cash went into a single cash management system, correct?" Mr. Genender: "Objection, form." Answer:

"Yes."

Question: "Okay. And the Debtors' accounting system would keep track of which entities would put cash into that accounting system, into that cash management system, correct?" Answer: "I'm not an expert on that system, so whether the system provided, quote, and I'm not sure what you mean by system, but whether the system provided the detail or individuals had to gather information, which is my understanding, and book entries, you know, they did it to the best of their abilities."

Question: "Okay. And if the Debtors took cash out of the system or bills were paid on their behalf, then the Debtors' books and records would record the fact that whichever particular Debtor was benefited by that owed a payable for that benefit, correct?" Answer: "It would be the ideal system. Whether the Sears -- I didn't audit their systems to know specifically how all the transactions were recorded."

In other words, Mr. Murphy's testifying that he can't figure out which Debtors owe money to which other Debtors or which Debtors are owed money, and he's worried that they may not be able to pay each other off, but he doesn't understand anything, apparently, about the cash management system because that wasn't within his area of expertise or his area of responsibility, I should say. So he

doesn't seem to understand, or the Debtors don't want to talk about the fact that these are all claims into and out of the cash management system, the centralized pot of money.

And, in fact, he had testified previously -- and I think I read that portion where he said the Debtors that needed money would take -- you know, there were -- there were borrowers and guarantors, and entities that needed money would take it out. But the Debtors recorded all this information, so it's available.

THE COURT: But I guess it's an integrated cash management system, so they net out an aggregate amount, but not Debtor by Debtor. It goes out of the system to whoever needs it, but it doesn't show -- it doesn't match up who gets it and who put it in.

MR. FOX: No, it does. Your Honor, it's the same as if you put your money in a bank. The bank then lends that money out to a whole bunch of people. You don't know who they are. And most of them hopefully pay it back.

THE COURT: But as far as intercompany claims go --

MR. FOX: Mh hmm.

THE COURT: -- I don't -- I don't know whether I have a claim against, if you bank at my bank, you or anyone else. I just have a claim against the bank.

MR. FOX: That's right.

THE COURT: On an integrated basis.

MR. FOX: And that's exactly what was happening here.

THE COURT: So how do you track the intercompany claims that way?

MR. FOX: They kept track of who put money, who took money out.

THE COURT: Yeah, but not -- out of the integrated system but not vis-à-vis each entity.

MR. FOX: That's all there was though.

THE COURT: I know. That's -- I guess that's why I'm saying that doesn't seem to be a ready way to determine which entity owes the other entity as opposed to sort of a general cash management system on a net basis.

MR. FOX: All the borrowers owe it to the bank, and all the -- all the --

THE COURT: Right.

MR. FOX: -- lenders are owed by the --

THE COURT: But if that's -- but the bank is consolidated. That's all of -- all of the Debtors.

MR. FOX: Mh hmm.

THE COURT: So to me, the testimony you were reading doesn't show an ability to break out which Debtor owes which other Debtor. It just shows which Debtor is net negative and net positive against a collective bank.

MR. FOX: That's right, and that's all you need to know because they --

THE COURT: Well, I'm not sure about that. If the money that K-Mart puts in goes 90 percent to Sears X and 5 percent to Sears Y and 2 percent to Sears Z, and 1 percent to (indiscernible), how do you work out the intercompany claims among those entities?

MR. FOX: Those entities that have a net payable have to pay money back into the centralized pot to the extent that they can, and they do. Then the creditors with the net receivable get to take their money out.

THE COURT: Of what, though? Because --

MR. FOX: Out of that centralized pot.

THE COURT: But then it's centralized.

MR. FOX: Yes. It's --

THE COURT: It's not -- the assets -- you're -- that presumes the substantive consolidation of the assets but not the liabilities.

MR. FOX: It's not -- but they kept track of it.

THE COURT: Of what?

MR. FOX: They kept track of, in a sense, the centralized bank account.

THE COURT: I get that.

MR. FOX: Right.

THE COURT: But --

MR. FOX: So --

THE COURT: Again, if you look at the assets of one of the Sears entities, in a -- in a non-substantive consolidation context, those assets would include the claims of that entity against each of the other entities because each of them -- it wouldn't matter if they were all solvent. But if they're not solvent, then it depends on whose claim -- whose claim is against who.

You know, if one entity on perhaps a net basis neither owes nor is owed on a consolidated basis through the integrated system but it owes a lot of money to an entity that can't pay it and is owed a lot of money by another entity that can pay it, you can see how that would be different than the flipside of that, which is it owes a lot of money to a company that it can pay, but it collects from a company that can't pay it at all.

MR. FOX: But the point is that the company's systems have already netted all those amounts.

THE COURT: Only as far as the company as a whole is concerned, not again each entity.

MR. FOX: No, they have netted it against each entity. And, in fact, the Debtors have said exactly that.

THE COURT: Well, that -- maybe I'm missing -- see, I thought --

MR. FOX: But --

THE COURT: What I took away from it is that there's a net amount owed to the bank.

MR. FOX: Yes.

THE COURT: And a net amount owed by the bank in some instances.

MR. FOX: Mh hmm.

THE COURT: But not entity by entity.

MR. FOX: Because they've netted it entity by entity, leaving claims against the bank or amounts owed to the bank.

THE COURT: But the --

MR. FOX: So --

THE COURT: I think the net -- entity-by-entity netting is as against each entity as against the whole, not as against each entity separately.

MR. FOX: But the point -- the ultimate point is that we know who has to put money in, assuming they have it, and who gets to take money out.

THE COURT: That's what -- that's the part I'm missing. I don't see -- if you're saying they take it out of the common pot, then again it seems to me that you're substantively -- you're presuming substantive consolidation of assets but not liabilities.

MR. FOX: No, because they know who owes what to the pot and who's entitled to what from the pot.

THE COURT: But it -- but it's the common --

MR. FOX: In other words, they know --

THE COURT: But it's the common pot. It's not the individual Debtors owing each other.

MR. FOX: I understand your point, Your Honor, but I'm suggesting -- and I don't know a quicker way to -- a better way to say it. We shouldn't -- we don't need to get hung up on which entity owes to which other entity when that's all been addressed within the system, leaving simple claims to and from the centralized pot.

THE COURT: But that may make sense if everyone gets paid the same from everyone, but that's not what happens here. So I think you would -- clearly, there would be creditors of individual entities that would want to say, I want to make sure my entity gets paid by the entity that I actually lent to. And actually, you don't really show any lending to an entity because it all goes through the common pot.

MR. FOX: What you ultimately want to wind up is getting the money back that you're owed.

THE COURT: But by -- but by whom? But the money back you're owed is by the bank. I don't --

MR. FOX: Yes.

THE COURT: Again, when I lend to Chase by putting my money in Chase Bank --

MR. FOX: Right.

THE COURT: -- I don't -- I get it back from Chase. I don't get it back from each individual account at Chase.

MR. FOX: That's correct.

THE COURT: But this -- but this is not that type of situation because you're talking about individual Debtors owing each other --

MR. FOX: That's --

THE COURT: -- as opposed to the -- to the company bank, which combines it all.

MR. FOX: Well, based --

THE COURT: And you have to unscramble all that to determine who owes who.

MR. FOX: Well, actually, based on Mr. Murphy's testimony, that's not exactly right that monies that -- if they needed money, they took it out. If they had money, they put it in. It all went into the centralized system. It -- Sears Roebuck didn't say, hey, K-Mart, you need some money? Here you go. If K-Mart needed money, it went to the treasury and took it out of the cash management system to pay its bills.

THE COURT: But who -- but who would it get paid from now?

MR. FOX: It would get --

THE COURT: You would say it would get paid from the main pot.

MR. FOX: Yes.

THE COURT: So how do you -- so that's the only intercompany claim you're counting.

MR. FOX: That's -- yes, and the intercompany -- the Debtors that have intercompany obligations have to put money in and -- to the extent that they have it, and the entities that are -- have intercompany receivables would then get to take their -- that money out. And if there's not enough, they would do it on a pro rata basis, which is what we would always do. You don't need to go back and look at every single transaction for the last five years or 10 years or, as Mr. Murphy seemed to think, 100 years because Sears is that old in order to sort this out. It's been sorted, and you can -- you can determine that.

Now, and in fact, you know, Mr. Murphy didn't seem to know that the Debtors don't have separate bank accounts with which to settle up intercompany accounts. They just leave it to the pot. So at Page 111 when I asked, "That disclosure statement says the Debtors believe there would be significant difficulties and enormous costs that would be borne by the estates in order to disentangle the prepetition intercompany claims on a Debtor-by-debtor basis, which would deplete the recoveries for all creditors and cause

unnecessary and costly delays in the confirmation of the plan and distributions to creditors; do you see that statement?" Answer: "Yes."

Question: "Why would -- as far as you know, why would it be necessary to disentangle the prepetition intercompany claims on a Debtor-by-debtor basis?" Answer: "On a Debtor-by-debtor basis -- because the numbers that are reflected in the books and records are on a net basis, they do not reflect those receivables that may or may not be collectible on a Debtor-by-debtor basis from each Debtor or non-Debtor entity in order to pay or which Debtor may be able to pay its particular payables. Those are net numbers."

Question: "Do any of the Debtor have separate bank accounts other than the concentration account?" Answer: "I don't know the answer to that question. I wasn't involved with the treasury."

Question: "Okay. Do any of the Debtors hold or have bank accounts that are used really for anything other than to have funds flow up to the concentration account?" Answer: "Again, I don't have firsthand knowledge of that."

He's making assumptions that he can know the due from and due to, and that if he knew that, somehow it would make a difference. And the point is it would not because that's not the way the Debtors operated, which he admits is

not an unusual way for companies like this to operate.

There is further -- he prepared -- and has -- and the Debtors have offered no analysis showing the cost to disentangle other than to say how difficult it would be. So when I asked him -- make sure I have the right page.

Question -- it's the top of Page 113. "Now, this statement refers to the enormous cost that would be borne in order to disentangle. Do you see that phrase, enormous cost?" The Answer: "Yes."

Question: "Is there an analysis that was prepared that shows what the cost would be expected to be?" Answer: "Not that I'm aware of."

So while they make the assertion that it would be an enormous cost, the never actually prepared any analysis.

Now, Mr. Murphy asserts -- not that he's qualified to do so -- that there's a 75 percent chance of substantive consolidation. That's his opinion, obviously, and he's not an expert as we've qualified as such. And, in fact, he really has no idea.

So when I asked him on Page 146 of his deposition, Question: "Let me ask you my question again, which is what's the basis for your assumption that there's a 75 percent risk of interstate, intercreditor litigation?" Mr. Genender: "Objection, form. Asked and answered." Answer: "I don't know how to answer it any way other than how I just did."

Question: "How did you come up with 75 percent?" Answer: "We basically -- we looked at the factors that we established based on experience and then putting all the challenges that we saw for executing a deconsolidated plan as substantial and made an approximation that there would be a 75-percent risk that should be applied."

Question: "Who is we? You said we." Answer: "The M-III team in discussions of the litigation challenges that would exist in trying to prosecute this."

Question: "Does the M-III -- do you have experience assessing the risk of litigation of substantive consolidation?" Answer: "I'm not a lawyer. I do not."

Question: "Does anybody else at M-III have experience assessing the risk of litigation of substantive consolidation?" Mr. Genender: "Objection, form." Answer: "I don't know."

So the result, though, based on that analysis, is that in a non-consolidation plan, K-Mart guarantee claims -- which our noteholders have, as do many others -- would get a recovery at K-Mart of, according to the Debtors, of 7.02 percent. And then the substantive consolidation plan, as purposed, the recovery would be 2.77 percent, and that's a significant difference, Your Honor. And that's why we're here.

Now, the -- there is an enhancement that was

finally negotiated -- I assume between the Debtors and the Creditors Committee. We were not party to any of those discussions -- that there's a 7.6 percent enhancement for K-Mart guarantees.

Now, the Debtors cite a number of cases where substantive consolidation was approved. Largely, those are lists for the purpose of establishing that these sorts of issues have been compromised. And most of them don't really -- first of all, it seems in most of those cases that the Debtors cite that the Creditors overwhelmingly seem to approve the plan, which is not entirely the case here. And -- but there's not a lot more information about the circumstances and whether the particular percentages or the ultimate determination of how the assets were divided up is set forth.

But too, there is some indication, and those are the Enron case and the WorldCom case. And in Enron, the Creditors received 70 percent of what they would recover without substantive consolidation from their own entity and plus 30 percent of what they would recover on a substantively consolidated basis. And guaranteed claims got a 50 percent recovery.

And that's a case where there were massive restatements, and you can take judicial notice of that. And the people running that entity were convicted of crimes,

involved in representing that entity, and you can take judicial notice of that. And yet the chance of substantive consolidation was only 70 percent, and guarantees got 50 percent.

In contrast, here the Debtors -- Mr. Murphy, without knowledge, is asserting there's a 75 percent chance of substantive consolidation and that the enhancement for guarantee claims would only be 7.6 percent, and otherwise we'd lose the balance of the value of that.

Secondly --

THE COURT: Of course, there was a lot more money to spend in Enron than there is here on that fight.

MR. FOX: Well, nobody got 100 cents.

THE COURT: No. But there was a lot more money to spend on the lawyers for fighting that issue, ultimately.

MR. FOX: Well, the point there as here was to obviate that fight, was to avoid that.

In WorldCom, the other one where the numbers are available in the decisions, the MCI pre-merger, unsecured creditors, received 42 percent of their allowed claims, and the MCI senior noteholders recovered 80 cents on the dollar, while the WorldCom unsecured creditors got new common stock in 18 percent of their allowed claims.

And again, that was a case where it was so hopelessly entangled that the Debtors claimed that they

could not prepare schedules and statements for each of the Debtor entities. And yet here, we're being told that there's a 75 percent chance and that the recoveries should be grossly limited.

It -- just as a matter of fact, as a matter of equity and exercising the Court's discretion, I would argue that there's a slim, if any, case for substantive consolidation and that what's been put on the table is grossly unfair, particularly to the guarantee claimants, and that may reflect why the vote by -- apparently by those creditors seems to be overwhelmingly negative.

THE COURT: Well, again, the numbers voting was overwhelmingly in favor as the dollar amount was less.

MR. FOX: I understand that, Your Honor.

THE COURT: That's how Judge Funk in Winn-Dixie evaluated it in terms of numbers of those actually voting as opposed to the dollar amount.

MR. FOX: I understand. I would simply say that the code requires both of those things. But to the extent that we believe -- and I think we do, or Your Honor seems to -- that those voting no, to reject the plan, were holders of guaranteed claims that, I think, does reflect their view of this, their concern about this, and the adverse effect that that has on them.

Now, I want to just talk briefly about the PBGC

settlement, and then I went to get back to the plan itself.

The PBGC settlement currently is that they would get a $97.5 million priority claim up from $80 million and an $800 million unsecured claim. The -- because of the (indiscernible) Fabricators case, which the Creditors Committee raised in their objection to the disclosure statement of the May plan, typically the view would be that the PBGC is not entitled to a priority claim. The explanation largely in this case seems to be that, nevertheless, it's an appropriate disposition of their claims because they were going to use their best efforts to cause KCD to give up its administrative claim of 140 -- of potentially $146 million on a post-petition basis.

The problem is there's nothing that I can find -- in the record at least, in either the Debtors' brief or the PBGC's -- that shows how the PBGC actually has the ability to control or cause KCD to actually do anything with respect to that claim.

So while there's the assertion that that's the case and that that's the justification, there's no indication that they're actually able to accomplish that. And our understanding is that because Transform bought those KCD notes, that if anybody had the ability to do that, it would be Transform, which we understand they did, not the PBGC.

So we're -- we just don't see the justification. But I think the more -- perhaps for this purpose, as I'll get to, more important point really is that the PBGC was willing to take the $80 million claim. And, yes, they traded that when the Debtors wanted to shift to substantive consolidation. But I'll come back to that in a minute when we talk about what plan you could or should confirm.

We also raised issues, which I don't think I need to belabor, about the appropriate classification of the claim and whether the Plaintiff was fair and equitable giving the way -- given the way the PBGC's claim has been classified.

But, I mean, the fact that it's joint in several claim, so are the guaranteed claims effectively. That really doesn't make much difference.

The point, though, that I think ultimately you can take away from this -- and this is an important point -- is that you can actually confirm a plan today assuming you deal with the other objections -- you're comfortable the other objections have been satisfied. And that plan is the toggle plan. There's no need to approve the substantive consolidation settlement because the toggle plan can be confirmed right now.

Now, that plan is a pot plan, and the creditors of each Debtor entity receive their pro rata percentage based

on the amount that their claims against whichever entity bear to the total of all claims against all of the Debtors. So, in effect, it follows what the Debtors have been doing all along, which is to keep all their money in one place and to have claims from various entities against that particular one pot of money.

The difference is that the holders of guarantee claims don't see their rights decimated. So, you know, they did the right thing to make sure that they would be protected, and now that's just being taken away from them under the terms of the settlement to which they clearly have not agreed but which will have a tremendous effect on them.

And the entire justification for the settlement is to avoid all this litigation, which so far has not occurred, and nobody seemingly wanted it to occur. The PBGC was opposed to it. The Creditors Committee expressed their opposition to it, to substantive consolidation. The Debtors were opposed to it too until they changed their minds.

So I'm not sure who's out there pushing in favor of substantive consolidation. But regardless, the plan, the toggle plan, is confirmable right now without the settlement, and I would suggest that it would become an abusive discretion to approve of a subs native consolidation settlement given the fact that the toggle plan has the votes and could be confirmed.

So there's no real necessity at this point to approve it other than to cause harm to the guarantee claims, help a class of claimants who I think fairly knew what they were getting into, knew that the guarantees were there, knew what they were up against, knew who they were trading with, and somehow now we've decided that under the guise of a substantive consolidation settlement of a non-existent dispute that somehow they should be favored at this point.

Two other points. We had raised an issue about the way in which Section 9.2(a) had been drafted and whether it really carried into effect the -- at least the 7.6 percent additional recovery from K-Mart guarantees. Finally, the Debtors corrected the plan, in this October 1 version from last Monday, and resolved that problem.

The last point relates to indentured trustees' fees and how those get treated under the plan. The plan says -- and it's different than the liquidating trust agreement. So the plan says that the Debtors and the Creditors Committee will negotiate over the treatment of indentured trustees' fees, but under no circumstances will indentured trustees' fees incurred in connection with objecting to the plan, to the disclosure statement, to the sale, or a bunch of other things -- there's a laundry list -- be paid.

The liquidating trust agreement then says that in

return for indentured trustees agreeing to make the distributions to their holders on behalf of the liquidating trust, that in payment for that service, they will be paid their fees not just for that service but all of their fees since the inception of the case -- except, however, not the laundry list of these other activities objecting to the plan, to the disclosure statement, the sale, etc.

If the Debtors want to pay indentured trustees the reasonable amount of their fees, we're all for it. We'd never say no. But when the Debtors start to pick and choose which activities they will or will not pay for that occurred during the case, we see that as a significant problem, and it has the potential -- we're not suggesting that that's the case here, but it certainly has the potential to cause indentured trustees to potentially temper their views about how they're going to do their jobs based on whether they will or won't get paid because of language like this.

And I -- we believe that Your Honor ought not start to head down that slippery slope and allow that kind of a provision to be put in the plan. If they want to pay, fine. Great. If they don't, then they don't have to. If they want to pay the reasonable fees, that's fine too. But when they start picking and choosing among specific issues that were litigated or not, then we see that as inappropriate.

And we would note that there are several indentured trustees on the Creditors Committee. They may well have participated -- we don't know, but they may well have participated in the determinations to cause the Creditors Committee to do those very things that the Debtors and the Committee say they don't want the Debtor to pay for. So we believe that provision should be changed.

But, as I said, short of that, Your Honor, we believe that Your Honor can approve a plan today, but that plan is the toggle plan. It is not the substantive consolidation settlement, which we do not believe there's either a basis for either as a matter of fact or, quite frankly, as a matter of law.

Thank you.

THE COURT: Okay. Does anyone who's objected to confirmation have anything more to say on substantive consolidation? No? So why don't we deal with that specific point with the Debtors' response?

MR. SCHROCK: Good afternoon, Your Honor. Ray Schrock, Weil Gotshal for the Debtors.

Your Honor, I'll try to take some of these just in turn in which they were made.

As to the arguments around the PBGC settlement that the Debtors had, you know, effectively changed their mind between February and May, there were ongoing

negotiations with the -- with the PBGC and, in fact, the unsecured Creditors Committee.

Those parties, we -- in the meantime, we were also doing the intercompany claims analysis which, as we highlighted, took approximately two and a half months just to review, you know, the majority of the post-petition period. And it became clear to us during that period that it was going to be, frankly, impossible to review the literally billions of transactions that went into -- that went into the intercompany claims pool.

And if I can summarize Mr. Fox's argument around the cash pool, as I heard it, I think it was because the Debtors used a centralized cash management system and consolidated their assets, they can't substantively consolidate. But I would submit to you that's the whole point. There was -- and as detailed in Mr. Murphy's declaration at Paragraphs 22, you know, there was a centralized cash management system. There was an ability for us to know if there's a net payable, you know, due and owing from the cash management system. But that's not the point. You have to know who it was due from and to in order to be able to track, you know, that analysis.

So as the uncontroverted testimony here supports, the intercompany balances are consolidated for all intercompany transactions recorded for each Debtor over

time, aggregated into one net balance of either a receivable or a payable for each Debtor that it collectively has with all the other entities, and is recorded as the net receivable or payable. That is the way this cash management system works.

Asking these estates with limited funds to go back and try and, you know, untangle that, frankly, we don't think that you can do it.

THE COURT: Well, Mr. Fox says you don't need to untangle it. You just -- you just, you know, if the cash -- under the cash management system, K-Mart is owed X and Sears Roebuck is owed Y and, you know, Sears Insurance Services is owed Z, you just have the money -- again, distributions run through that system and net it out as to each estate.

MR. SCHROCK: That, to me, sounds like substantive consolidation. I mean, when I pull it apart, you're talking about a centralized pool of assets from which everybody has either a net payable or receivable due from. I don't understand how you can call it anything other than that. I mean, the receivables and payables were -- they were -- they were substantively consolidated for all intents and purposes. You just have -- you have to have a transaction net due and owing to the actual entity. Otherwise, I think that, you know, you're having parties act for -- as parties becomes insolvent, your acting parties act as conduits for,

you know, frankly, fraudulent conveyances, preferences, and a whole mess of other items that we noted in our brief and as well as Mr. Murphy noted in his declaration.

There's little doubt here that the creditor entanglement prong of the Augie/Restivo test is the one certainly that we found to be most prevalent here, creditor reliant. I think there were facts that were going both ways.

We did outline on Page 136 of our brief for several pages, you know, what some of those tos and fros are, but I will say that what's really missing from Mr. Fox's argument and was missing from the record is that Wilmington Trust had the opportunity and the ability to present contrary evidence. It is our burden to prove up the settlement within a lowest range of reasonableness, but there's nothing here as there were in other cases in which he cited about parties going and arguing that you can actually pull these entities apart. And I submit it's just not possible. You know, this is a 125-year-old company. It has been operated on a consolidated basis, as far as we can tell, forever. And certainly since it's merger with K-Mart in the early 2000s, it's been operating out of three primary entities.

But as to the percent chance that Mr. Murphy gives substantive consolidation, Mr. Murphy's not a lawyer. Mr.

Murphy takes the facts, presents those facts, and then it's up to the lawyers to make the arguments around how those facts are then applied to the law. That is what we've done in the context of this brief, and that's certainly what the parties did in negotiating the premiums that are payable on account of guarantee claims.

But, Your Honor, there's little doubt that the facts are here for a sub con. They're uncontroverted. There's some deposition testimony that has been highlighted, I think in a rather confusing manner, to suggest that Mr. Murphy didn't understand the nature of a sub con analysis. I think that his -- certainly his declaration suggests otherwise.

As to the Trustee, we're happy to have the Trustees rely, frankly, on their charging lien if that's the way the Court wants to -- wants to deal with that issue. We are -- we're also, you know, not in a position where we can, you know, go forward with a toggle plan.

And I think what Mr. Fox really meant on the toggle plan was confirm a plan for the Debtors that are able to, and for everybody else, I guess they liquidate and go into a Chapter 7.

But the -- you know, the toggle plan under -- you know, on Page 50 in Section 9.2(e) notes that in the event the bankruptcy court does not approve the plan settlement,

the plan shall, subject to the reasonable consent of the PBGC and the Creditors Committee revert to a joint plan of liquidation for each Debtor, a toggle plan.

Now, the PBGC is here. They've certainly made clear to us, and one of the reasons that we couldn't strike the deal around the non-sub con plan is because the PBGC in the Court's settlement discussions indicated that they would not consent to the toggle plan. They're the largest creditor of these estates. It's certainly something that we took into account in formulating the settlement. But I'm happy to answer any other questions the Court has.

THE COURT: What is -- what is or was the power of the PBGC to cause KCD to pursue the $146 million administrative expense claim?

MR. SCHROCK: Your Honor, as I recall, there's three directors that are on the KCD board. The one independent director that is on KCD serves at the pledger of the PBGC. We're still working with them around getting the actual -- getting the admin claim, you know, waived. We're confident that, in fact, we will. But, you know, those are the -- you know, there's been some issues just around, frankly, just some of the legal fees that have incurred at KCD, so there's ongoing negotiations associated with that. But they've certainly been holding up their end of the bargain as to -- as to KCD. But that is a waivable

condition, certainly, too, to the effective date as well.

THE COURT: Which is?

MR. SCHROCK: The waiver of the KCD administrative claim.

THE COURT: Well, except the feasibility estimates don't have $146 million in it.

MR. SCHROCK: That's correct, Your Honor. That's not our anticipation as to how that's going to play out, and we've certainly been working toward that. And, in fact, it's just a matter of time before we -- before we get that claim waived.

THE COURT: Okay. The other two directors have indicated that they're prepared to approve the waiver?

MR. SCHROCK: That's correct, Your Honor.

THE COURT: Okay. Okay.

MR. SCHROCK: Okay.

THE COURT: Someone behind you wants to speak.

MR. RAYNOR: Good afternoon, Your Honor. Brian Raynor of Locke Lord on behalf of the Pension Benefit Guaranty Corporation. I just wanted to add a little bit of flesh to the nature of the waiver.

Prior to the bankruptcy case, a number of Debtors and PBGC entered into agreement where PBGC was able to appoint, to identify or select one of the three managers at KCD, the independent manager. Also --

THE COURT: And that was part of a pre-bankruptcy settlement with the PBGC.

MR. RAYNOR: That's correct, but as of the bankruptcy filing and as of today, that independent manager is still there, and KCD is not a -- is not a bankrupt entity.

THE COURT: Right.

MR. RAYNOR: Also, the way the structure works is that there are essentially two creditors at KCD. One was the holder of the KCD notes, and one was Pension Benefit Guaranty Corporation by virtue of it joining several claims. So in connection with the sale, the eventual noteholders waived their claims to any admin claim that was approving at KCD, which leaves PBGC as the only entity at that claim, so there was essentially a derivative claim for the rights of the administrative expense claim at KCD, and there are definitely disputes around the bankruptcy filing as to PBGC's asserting that amount, and it was one of a number of disputes with the Debtors that was eventually settled pursuant to the PBGC's settlement.

And I'll also say that there have been discussions with the Debtors about making sure that that claim is waived, and those are -- assuming that the plan settlement goes effective -- that is not going to be a problem. PBGC will be lending its support to that waiver any way possible.

THE COURT: As the only creditor of KCD.

MR. RAYNOR: That's correct.

THE COURT: Okay. And was Mr. Schrock correct that PBGC is not consenting to the pivot, to the toggle plan?

MR. RAYNOR: That's correct, Your Honor. We submitted a ballot in support of the plan, but the toggle would be --

THE COURT: I managed to use two financial clichés in one clause, but --

MR. RAYNOR: That's correct, Your Honor.

THE COURT: Okay. All right. Thank you.

MR. O'NEIL: Just really quickly, Your Honor, Sean O'Neil, Cleary Gottlieb on behalf of Transform. Actually, Transform owns the KCD notes, so I just -- I just wanted to make it clear that Transform, as the holder of the KCD notes, is also a creditor of KCD. I don't -- I don't think there's any dispute about that. I just wanted --

THE COURT: But I thought -- well, I was just told that it's part of the sale, the right to assert that -- or to look to that claim was waived.

MR. O'NEIL: Correct.

THE COURT: Okay.

MR. O'NEIL: But --

THE COURT: So you're creditor, but you're not

looking to that asset.

MR. O'NEIL: But we've waived the -- we've said that we would do the same thing that PBGC has said it will do.

THE COURT: Okay.

MR. O'NEIL: Thank you, Your Honor.

THE COURT: All right.

MR. DUBLIN: Good afternoon, Your Honor. Phil Dublin, Akin Gump, on behalf of the Committee. I just want to touch on two points and expand on things that Mr. Schrock said, first with respect to substantive consolidation.

I think Mr. Fox's description of the cash management system and its impact on substantive consolidation oversimplified the issue. Each time money goes into the centralized cash management system, money then goes out somewhere. And Mr. Schrock touched on this, whether the cash management entity is a mere conduit and you have to then determine where each dollar went and who each dollar went in from and where it went to awards to determine proper intercompany claims is an issue that is being settled as part of the plan settlement.

And if you ignore that issue, as Mr. Schrock alluded to, when you have every entity inside the structure insolvent and you have K-Mart, for example, sending a dollar into the cash management system and the cash management

system sending that dollar out to Sears, Sears Roebuck, K-Mart can look through for the immediate transferee of the initial transferee to try to get back the value that it transferred out, creating fraudulent transfer claims all over the places inside of the Sears corporate structure, which creates the same intercompany conundrum as if the centralized cash management system didn't exist.

So I think just looking at money in and money going out and only looking at the cash management entity as to who owes moony to the various entities is just not giving the proper oversight analysis with respect to the issue at play.

THE COURT: But you don't know who owes money to various entities. You owe -- you know what the cash management system shows the cash management system owes to each entity.

MR. DUBLIN: And that's the point, Your Honor. As K-Mart puts money in, that's a fraud -- that -- as a -- into the insolvent cash management entity, that's a fraudulent conveyance because it's not getting it back. It's putting 100-cent dollars in, and it's getting an unsecured claim back. That's not worth the value that it put into the cash management system.

The cash management system then sends that dollar out to another entity inside the structure. Then K-Mart

would have a claim to the immediate transferee of the initial transferee, the initial transferee being the cash management entity, and the immediate transferee of the cash management entity being somebody else inside the Sears structure creating another intercompany claim.

THE COURT: And why wouldn't the ultimate, just netting through the cash management system itself, solve that problem, just saying that --

MR. DUBLIN: Because then you get the different -- then you have the entity that put in the 100-cent dollar is not getting back the value for its 100-cent dollars because it's then looking -- the cash management entity is then looking to Roebuck to pay back what it owes, and Roebuck doesn't have 100-cent dollars to put back in, so you have the creditors being disadvantageous.

THE COURT: Or it would be collecting from one of the other ones that owes -- that is healthier.

MR. DUBLIN: Correct. Then you have entities all competing for that same pot of cash, and the entity that put the money in not getting back what it would otherwise be entitled to.

THE COURT: Okay.

MR. DUBLIN: On the point with respect to the Trustee's fees, that was a point that was --

THE COURT: It seems like it should just be the

charging lien.

MR. DUBLIN: The way it was worked out was that if the trustee wants to help with the distractions, this is what they can get. If they don't want to help out, they don't have to take it, and they can execute on their charging lien.

THE COURT: Well, when you say help, I mean, it's more than just makes the distributions. It's also not objecting to confirmation (indiscernible).

MR. DUBLIN: Exactly. And also trying to figure out where all the money goes, and working with DTC, and making all the appropriate --

THE COURT: So --

MR. DUBLIN: -- distributions to various noteholders.

THE COURT: Let me make sure I understand then. The Debtor is prepared to say that -- and the Committee is prepared to support not only the charging lien but also the actual distribution money being paid on top of the charging lien, for distribution services. So if they're going to be facilitating the distribution, they get paid for that up front, as opposed to a charging lien? And they have a charging lien for everything else?

MR. DUBLIN: Well, they would -- they would get their -- they have two things, that the indenture trustee

would have there to help facilitate distributions when they're actually made, and none of the money that would go to pay Trustee fees would happen (indiscernible) actually have money to make distributions.

One, they would be paid for their costs and expenses occurred during the case in consideration for being the disbursing agent for the trust when noteholders are entitled to distributions. And then the de minimis -- the additional costs that are incurred in actually making those distributions, they would be paid as well. Ultimately, you have a difficult construct of figuring out how you're going to make distributions to public noteholders without the use of the trustees, which they're not obligated to do.

And the -- if a trustee doesn't want to act as the --

THE COURT: But I'm sorry, just on the first point there.

MR. DUBLIN: Yep.

THE COURT: I want to make sure I understand. They get -- they get their reasonable fees and expenses from what's incurred during the case for acting as the -- facilitating distributions. But that -- would that include, for example, objection to the disclosure statement?

MR. DUBLIN: No.

THE COURT: No.

MR. DUBLIN: It would not.

THE COURT: So what would it include?

MR. DUBLIN: It's --

THE COURT: Just being there to field phone calls?

MR. DUBLIN: And being the trust -- like the role that the Trustee plays.

THE COURT: Just as the normal Trustee.

MR. DUBLIN: Correct.

THE COURT: Okay.

MR. DUBLIN: Right, the administrative function that the Trustee plays.

THE COURT: Okay. So it wouldn't cover -- let's assume that instead of objecting to the plan, the indentured trustee not only didn't sit quietly but actually spent $100,000 writing a brief in support of the plan, that wouldn't have been compensated either because that's not your normal thing?

MR. DUBLIN: Nobody did that --

THE COURT: Well --

MR. DUBLIN: -- so we didn't have to -- it's not an issue that had to be faced by the estate.

THE COURT: Okay. All right.

MR. DUBLIN: Thank you, Your Honor.

THE COURT: Okay.

MR. FOX: Your Honor, if I may.

THE COURT: Sure.

MR. FOX: Your Honor, there's a few of Mr. Schrock's points in terms of the ongoing review. The written analysis, and this is again in the deposition testimony of Mr. Murphy, was finished on April 17th, which is the day they filed the non-consolidation plan. Mr. Murphy did testify that they continued to do some additional work and basically answer questions after that. Their primary analysis of the, you know, the intercompany accounting was done at that time.

THE COURT: But that's the post-petition --

MR. FOX: Yes.

THE COURT: -- analysis? Yes.

MR. FOX: Yes.

THE COURT: Okay.

MR. FOX: And basically, I mean, although he said they didn't actually extrapolate, that's effectively what they did. There wasn't --

THE COURT: But to me, you are pointing to the fact that one of the reasons that the parties moved to a substantive consolidation plan and then a substantive consolidation settlement was because of the effect of non-consolidation on various Debtors where there would be a larger administrative insolvency.

And I guess I'm less troubled by that because it

would seem to me that in the normal case where that doesn't pertain, you wouldn't -- you wouldn't get into these types of issues because the transfers actually do net out in 100-cent dollars whereas in an insolvency situation, they don't. Plus, what you're spending, 100-cent dollars, to fight over fractional-dollar disputes, and that doesn't make sense to me either.

MR. FOX: Well, I guess it depends whether they're your fractional dollars in dispute --

THE COURT: Well --

MR. FOX: -- or somebody else's.

THE COURT: I appreciate it's a different on the upside between 7 percent and 2 and --

MR. FOX: 2.7.

THE COURT: -- 2.7 percent or 2.77 percent. And albeit, that’s a difference of $23 million, but that’s on the -- the 2.7 is, of course, a bump up from 1.85 and you’re spending several million dollars to have that fight.

MR. FOX: Well, I would look at it this way, and I think this is -- in my view, there’s a fundamental difference between this sort of a “settlement” and a settlement of a two-party dispute, if you will.

THE COURT: Well, no, I appreciate that, but the caselaw is clear that you can settle substantive consolidation with some people who are unhappy about it.

MR. FOX: Well, okay, so --

THE COURT: It just has to be reasonably fair.

MR. FOX: Well, A, I would suggest this is not, but more importantly, Your Honor, I don't think that that settlement of the issue of substantive consolidation allows the Debtors to throw in everything including -- every other problem in the case including the kitchen sink and then call it, well, substantive consolidation because that --

THE COURT: You mean the PBGC settlement.

MR. FOX: Well not just -- laying aside that for a minute, just the fact that some entities are administratively insolvent and others may not be, okay, that's a problem, but does that justify substantive consolidation? Is that one of the factors that the Second Circuit identified in Augie/Restivo?

THE COURT: Well, if you run out of the money -- well, actually, it is identified in the cases that have that issue. The Republic case and the Winn-Dixie case both talk about cost of the litigation over substantive consolidation, rendering the whole issue academic.

MR. FOX: But -- well, the cost is one thing. But whether one estate is dealing with the administrative insolvency of certain Debtor entities is a whole different question.

THE COURT: I understand, but --

MR. FOX: So --

THE COURT: But again, it -- I mean, it's not like Kmart is rolling in dough.

MR. FOX: Well, by all accounts, they eventually will be and we all hope --

THE COURT: Well, eventually is one thing, yes.

MR. FOX: -- for that day.

THE COURT: But not in the cost of litigating these. I'm talking about today, litigating these issues.

MR. FOX: Well --

THE COURT: And --

MR. FOX: There was --

THE COURT: You say that the Court -- the Debtors can't wrap all of these problems into a settlement and I agree with that, but the PBGC settlement at this point is premised upon substantive consolidation under the plan, and if you add $146 million of admin costs, that just --

MR. FOX: Well, the PBGC --

THE COURT: -- a deal killer.

MR. FOX: I don't think the PBGC settlement, despite counsel's representation, can really be used as an excuse to stay with substantive consolidation. The -- what the plan provides in 9.2E is that the PBGC would have to approve it and it would have to be reasonable, determining whether to approve it or not.

Given the fact that the PBGC already entered into a settlement in February -- we have signed terms sheets that are in the record agreeing to not -- in fact, they didn't want to consolidate -- for them to now say oh, we do, I think it would be a little hard for them to suggest that they're going to object to it based on -- that they would be reasonable in refusing to agree to that. If Your Honor approves the PBGC settlement separately, so be it. We can still have the toggle plan.

THE COURT: Well, no. They have the right to veto the toggle plan.

MR. FOX: They don't have an absolute right. They have to act reasonably and I'm suggesting they would not, especially given the fact they previously agreed to this and, as counsel admitted, they voted in favor of this in every class. That's the class the Debtor is relying on.

THE COURT: But that's circular because they voted in a situation where they have this consent right. It's not like they voted and then it could be imposed on.

MR. FOX: But the exercise has to be reasonable.

THE COURT: Well, why is it unreasonable for PBGC to say, we don't want months of litigation and several of these Debtors to go into Chapter 7?

MR. FOX: No, no, no. There would not be months of litigation and they would not go into a Chapter 7. You'd

confirm the toggle plan.

THE COURT: No, but the toggle plan is just -- it's only for those entities, because it's an entity by entity plan.

MR. FOX: It's all of the --

THE COURT: It's only for the entities that can actually confirm the plan. I would have to have whole new hearings. I mean, the plan actually contemplates that, is that you give notice and then you have, like, the whole separate hearings or objection to the entity by entity plan.

MR. FOX: Well, the Debtors' confirmation brief dropped a footnote to suggest something like that, but I don't think the plan itself said --

THE COURT: Well, no. I think it actually is worded that way.

MR. FOX: Your Honor, the vote --

THE COURT: I mean, how could I confirm individual plans without going through the individual confirmation standards for each entity, including A9 and A11? I don't think I could.

MR. FOX: You -- that's right, Your Honor, but the funds -- just like the funds are available to confirm the consolidated plan, the same funds are available. Instead of being gifted, they'd be lent as -- the plan provides that the solvent entities would lend to the insolvent in order to

get this done. There are --

THE COURT: And how do we know which is which, then? So we're back to that same litigation again.

MR. FOX: No, it's not litigation. They'd either have the funds at the effective date to make the payment of the administrative expense --

THE COURT: I can pretty much guarantee you that when each individual case was noticed for confirmation, there would be someone equally talented as you on the other side saying, my Debtor is actually a net winner when you do the analysis. And they're going to be paying me, not Kmart.

MR. FOX: If they can make that case, God bless them, but I don't --

THE COURT: Well, that's the point is that --

MR. FOX: No --

THE COURT: -- we'll be spending all the next several months doing that with the litigation costs when $1 or $2 million in the settlement means a lot.

MR. FOX: Your Honor -- well, losing 60 percent of what would otherwise be one's recovery means a lot and --

THE COURT: Well --

MR. FOX: -- and the --

THE COURT: If you assume that that's actually what you would recover.

MR. FOX: Well, based on -- well, we're all basing

everything on the Debtors' assumptions. Now, if the Creditors' Committee hits a home run, then maybe it'll be a lot more than the Debtor assumed and lower percentages will nevertheless not matter. The toggle plan itself, just to be clear, it's a pot plan to begin with and it -- and the Debtors effectively lend to each other to make sure they're all administratively -- to pay their administrative expenses.

In effect, it contains elements of substantive consolidation already. We're not challenging that. But this is just -- the sub con settlement is just a bridge too far. It's wildly excessive, particularly under these circumstances. Now, let me just move on because I appreciate the opportunity to respond to the points.

The point about the netting and Mr. Schrock said that the Debtors can't determine who owes what to whom, the point again is, you don't need to. And in fact, the toggle plan, the pot plan, you don't need to, either because everybody's just getting out of the pot. The fact --

THE COURT: But, again, in fact you just said it. That's in essence, a substantive consolidation.

MR. FOX: No, well, what it really does --

THE COURT: On the asset side.

MR. FOX: Well, you could view it that way, but effectively what it does is follows exactly the way the

Debtors ran their business and the way everybody did business with the Debtors. It's, in a sense, the fairest way because it follows what was going on and what everybody was dealing with. The --

THE COURT: But it's a black box, so how could you say everyone was dealing with it? It's a black box. It goes in. Everyone was dealing with it on the assumption that each of these entities would be good for the whole amount.

MR. FOX: That's why people extend credit.

THE COURT: So they didn't account for each transaction as to who benefitted from what. But now that it matters, it seems to be that a more nuanced approach is appropriate, which is what they've come up with.

MR. FOX: Well, what they've come up with is an approach that takes it all out of the guarantee claims.

THE COURT: Well, it gives the guarantors something.

MR. FOX: Not much.

THE COURT: Well --

MR. FOX: And it doesn't even reflect if there's a 25 percent chance. It doesn't even reflect that. And compared to 50 percent in Enron, I mean --

THE COURT: I'm sorry, why doesn't it reflect the 25 percent?

MR. FOX: Well, it's a 7.6 percent enhancement. If you have -- for a Kmart guarantee claim, now that they fixed the plan.

THE COURT: Well, it goes --

MR. FOX: 9.2(a)(7), I think.

THE COURT: It goes from -- I'm sorry, from 7.7 to 11.6?

MR. FOX: I'm not sure what you're looking at, Your Honor.

THE COURT: The recovery.

MR. FOX: Oh, the disclosure statement?

THE COURT: Well, the various charts. They're all basically the same, but it -- before the settlement, the recovery by the non-ESL guarantee claims would be $7.7 million projected and under the settlement, it goes to 11.6. So that's a little over $4 million.

MR. FOX: Well, I'm not sure how they came up that. As I say, the --

THE COURT: Well, the --

MR. FOX: -- plan itself provides for the 7.6 percent enhancement on the recovery. So putting aside the dollar amount, that's the enhancement to negate the adverse impact on the guarantee claims that we have against Kmart that we would lose. That's what the plan provides. I can't speak to their analysis. And their analysis makes various

assumptions.

THE COURT: I'm sorry. Under a deconsolidated plan, it's a little under $31 million, is the recovery. They discount that by 75 percent to $7.7, so they are giving you the 25 percent. You don't think of it as a gift, but they're giving you the 25 percent and then they're adding on top of that $3.9 million which is about 10 percent more of the $30.9 million, a little over that, 11 percent more.

MR. FOX: Yeah, I'm not sure how they --

THE COURT: So totally -- so the total amount is like 33 -- I'm sorry, 36 percent recovery.

MR. FOX: Your Honor, I'm not sure how -- I don't have that in front of me. I'm not sure how you're getting --

THE COURT: Well, I mean, I think that --

MR. FOX: But I --

THE COURT: I mean, that's -- I think I'm doing the math right.

MR. FOX: That may be. All I'm saying is that when you look at the plan itself in 9.2(a)(vii), the enhancement is you get, then, 7.6 percent of your recovery on account of your guarantee claim. You don't get 25 --

THE COURT: Oh, well, yeah, because you're not expected to get anything anyway. I mean, you expect to get a very little amount, but the enhancement isn't -- I mean,

I'm just focusing on the fact that you're saying that the bump up here is miniscule. Maybe in terms of dollar amount it is small, but you're talking about small projected recoveries anyway because the Debtors are being conservative here on litigation recoveries and again, it's a 25 percent recovery and then you add another 10 percent onto what you'd be getting under a consolidated plan.

MR. FOX: Well, as I said, I was referring to the percent of the -- recovery percentages. If I could, I just want to address the last points about the Trustee's fees that Mr. Dublin raised. In order for a Trustee to exercise his charging lien, it must make the distribution.

THE COURT: Right.

MR. FOX: Otherwise, it can't assert.

THE COURT: Right.

MR. FOX: And it's entitled under the rules to receive the distribution for exactly that purpose.

THE COURT: Right.

MR. FOX: So --

THE COURT: No, but they're prepared to pay on top of your charging lien, so you don't have to hold back the distribution -- it's really for the benefit of the noteholders -- your distribution charges.

MR. FOX: Yeah.

THE COURT: Your normal charges --

MR. FOX: We --

THE COURT: -- for being an indentured Trustee, so that's on top of the charging lien.

MR. FOX: Right. Well, ordinarily the fees to actually do the distribution or charge separately to the estate --

THE COURT: No --

MR. FOX: -- and they're paid. But what the Debtor -- what the plan and the liquidation trust agreement provide is much more than that.

THE COURT: I understand, and I don't -- I agree with you. I think the deathtrap aspect of it isn't appropriate, but I will interpret that provision to say that if the Trustee just does its normal duties, the noteholders won't be charged for those through the charging lien. They'll pay you directly for that so that every dollar that you get after that you can pay them or assert some other charging lien for whatever else you've got in the case.

MR. FOX: So it's just the actual distribution cost --

THE COURT: Well, I don't know if it's that. I mean, there may be other things your client did during the case, like field phone calls or keep lists or, I don't know. I don't know what else to --

MR. FOX: Right.

THE COURT: Indentured Trustees normally get paid a ridiculously low amount of money for those types of things, so I'm assuming it's not a lot, but maybe they do something. I don't know.

MR. FOX: Well, okay, because the language that's in the --

THE COURT: But --

MR. FOX: -- now is not that --

THE COURT: I agree with that.

MR. FOX: That's everything they did. If they spent 1,000 hours reading every document that was filed --

THE COURT: I agree.

MR. FOX: -- but never took a position, the plan and the liquidation trust agreement would pay them for all of that work.

THE COURT: Well, that doesn't make sense.

MR. FOX: Well, that's what it provides.

THE COURT: Okay. All right.

MR. FOX: Thank you, Your Honor.

THE COURT: Okay.

MR. SCHROCK: Your Honor, just really quickly for the record. I think it's important to note that when Wilmington Trust makes these arguments, as they noted, they're making for the 2L notes which are payments subordinated, the $89 million that's at the bottom tranche,

so as you may recall --

THE COURT: So the recoveries are going to be low to begin with.

MR. FOX: Your Honor --

THE COURT: They're subordinated as liens and to other debt, but --

MR. FOX: Only the liens are subordinated.

THE COURT: Yeah.

MR. FOX: The debt is not.

THE COURT: But we're talking about projected low recoveries for all unsecured creditors.

MR. FOX: Right.

THE COURT: So to complain that it's only a 7.7 percent recovery, it's lower for the other unsecured creditors by about 50 percent of that, so it's not -- I think you're mixing apples and oranges, Mr. Fox, as far as the bump up as part of the sub con settlement is concerned. No one else has a substantive consolidation issue? I don't think so. All right. I...

MR. KRELLER: Your Honor, Thomas Kreller from Millbank, LLP for Cyrus Capital.

THE COURT: Okay.

MR. KRELLER: I actually do have a few other issues.

THE COURT: No, I know, but I'm wondering if you

have a substantive consolidation --

MR. KRELLER: I don't have a substantive --

THE COURT: Okay. So I'm going to rule on that issue now. I have before me in the plan a proposal under which -- under the plan the Debtors would be substantively consolidated under the Court's general equitable powers, which is well recognized in the Second Circuit including In RE: Augie/Restivo Baking Company, Limited, 860 F.2d. 515, 518 Note 1 (Second Circuit, 1988).

Substantive consolidation is the effect of consolidating the assets and liabilities of multiple Debtors and treating them as if the liabilities were owed by and the assets held by a single legal entity. In the course of satisfying the liabilities of the consolidated Debtors form the common pool of assets, other company claims are eliminated and guarantees from co-debtors -- unsecured guarantees, that is -- are disregarded.

In RE: Republic Airways Holdings, Inc., 565 B.R. 710, 716 (Bankruptcy S.D.N.Y. 2017) and In RE: WorldCom, Inc., 2003 Bankruptcy Lexus 1401 (Bankruptcy S.D.N.Y. October 31, 2003).

While the Court has considerable discretion in ordering substantive consolidation, the Circuit has made it clear that the power should be used sparingly because of the possibility of unfair treatment of creditors who have dealt

solely with that Debtor without knowledge of its interrelationship with others. Chemical Bank, New York Trust Company v. Kheel, K-H-E-E-L, 369 F.2d. 845, 847 (Second Circuit 1966).

Courts apply multiple factors in determining whether substantive consolidation is appropriate but the Circuit in Augie/Restivo distilled those considerations into two primary or critical inquiries phrased in the disjunctive, i.e., whether “creditor dealt with the entities as a single economic unit and did not rely on their separate identity in extending credit,” or separately, the affairs of the Debtors are so entangled, consolidation will benefit all creditors. Augie/Restivo, 860 F.2d. 518.

Substantive consolidation, given its equitable basis is not a black and white or all or nothing result. The Courts look at whether the proposed consolidation will yield an equitable treatment of creditors without any undue prejudice to any particular group, In RE: Food Fair Inc., 10 B.R. 123, 127 (Bankruptcy S.D.N.Y. 1981) and Republic Airways Holdings, 585 B.R. at 716 and should apply the remedy in a practical manner.

Thus, it quoted, “It is well accepted that substantive consolidation is a flexible concept and that a principal question is whether creditors are adversely affected by consolidation, and if so, whether the adverse

effects can be eliminated or otherwise dealt with," id., Page 717.

It is also the case, consistent with the point I just made that substantive consolidation can be proposed in the form of a settlement of substantive consolidation issues or issues pertaining to substantive consolidation under Bankruptcy Rule 9019 and there are numerous cases that apply the substantive consolidation in the context of aw related settlement analysis that is applying the so-called iridium factors or TMT Ferry factors applicable to analysis of a proposed settlement as set forth in In RE: Iridium Operating, LLC, 478 F.3d. 452, 462, citing among other cases, In RE: TMT Trailer Ferry, 390 U.S. at 424.

In the substantive consolidation context, in addition to the Republic Airways case that I've previously cited, such an approach applying a settlement analysis as well as substantive consolidation analysis was undertaken in In RE: Winn-Dixie Stores, 356 B.R. 239 (Bankruptcy N.D. Florida 2006) as well as in a number of reported and unreported decisions cited in the Debtors' brief -- reply brief in support of substantive consolidation, albeit that those settlements did not have extensive analysis.

They include, though, In RE: WorldCom, Inc. that I previously cited as well as the Enron confirmation ruling that is cited in the Debtors' reply memorandum where a

substantive consolidation analysis which at the confirmation hearing took up a lot of time and argument, was resolved on a consensual basis except for some relatively modest remaining objections and dealt with in about a page-and-a-half of a 200-page decision.

Obviously, in approving or in considering a settlement, particularly in the context of substantive consolidation being among the settled issues, the Court needs to ensure that the settlement isn't unduly at the expense of a party or parties who are not on board with the settlement and who are affirmatively objecting to it. Nevertheless, I can clearly approve a settlement where not every affected creditor consents.

That's the case under the substantive consolidation caselaw as well as the settlement caselaw, even where a class does not accept a settlement. Again, see In RE: Winn-Dixie Stores, 356 B.R. at 249.

The settlement here is complicated by the fact that it is not only a proposed settlement of substantive consolidation issues, or issues pro and con in favor of substantive consolidation, but also incorporates a complex settlement between the Debtors and the PBGC, their largest creditor.

That settlement as originally proposed by the Debtors and PBGC in a terms sheet did not contemplate

substantive consolidation, but as ultimately proposed, while it contains or contemplates the possibility of a non-substantive consolidation plan, i.e., the so-called toggle plan, a switch to the toggle plan requires the consent not to be unreasonably withheld of PBGC and the Official Unsecured Creditors' Committee which joined in the PBGC settlement in its ultimate version.

The PBGC in the settlement substantially compromises its claims and looks for one consolidated recovery. In addition, and importantly here, the PBGC agrees to use its best efforts to cause a non-Debtor subsidiary of the Debtors, KCD, not to pursue a $146 million administrative expense claim against the Debtors.

I believe on the record before me, it is clear that PBGC not only has the requisite influence to cause that to occur given that the independent director of KCD was subject to the nomination by PBGC and PBGC is currently the only creditor of KCD that would have an interest through KCD in such a claim or on KCD pursuing such a claim. Clearly, if PBGC, as is stated on the record today, informs KCD's board that it has no desire to have KCD collect on their claim, it's highly likely that the KCD board would not pursue the claim.

The record of this confirmation hearing generally makes it clear that the Debtors' current cash position would

not let them emerge from bankruptcy until various events occur in the future that would enable them to pay allowed administrative expenses in full or as agreed by the administrative expense creditors holding allowed administrative expenses, in compliance with Section 1129(a)(9) of the Bankruptcy Code. That is the case even without a $146 million administrative expense claim.

To add that administrative expense onto the Debtors' balance sheet would raise very serious feasibility issues for these Debtors, in all likelihood causing most and perhaps all of them, including the entity that apparently the objector, Wilmington Trust, looks to most prominently, the Kmart Debtors, to be rendered administratively insolvent.

So the PBGC settlement is important. It appears, based on the record before me, that the final version of that settlement was negotiated with the administrative claim position of these cases or these Debtors well in mind. I believe that was a good faith and rational and reasonable basis for the negotiation of the settlement and that the two are, in fact, properly linked, that is the substantive consolidation settlement and the PBGC settlement.

PBGC's counsel has represented that it is not prepared to waive its right to object to switching to a debtor-by-debtor so-called toggle plan and given the facts

before me, that insistence does not appear to me to be unreasonable.

In evaluating a settlement, the Court considers, as laid out by the Second Circuit in Iridium and WorldCom and TMT Trailer Ferry, one, the balance between the litigation's possibility of success and the settlement's future benefits, the likelihood of complex and protracted litigation with its attendant expense, inconvenience, and delay, including the difficulty in collecting on the judgment, the paramount interests of the creditors including each affected class's relative benefits and the degree to which creditors either do not object to or affirmatively support the proposed settlement, whether other parties in interest support the settlement, the competency and experience of counsel supporting and the experience and knowledge of the Bankruptcy Court judge -- well, this is on appeal, obviously -- reviewing the settlement, the nature and breadth of releases to be obtained by officers and directors and the extent to which the settlement is the product of arm's length bargaining.

Obviously, in any multifactor test, certain factors simply don't apply and some factors may, under the particular -- or in the particular context, be more important than others. In addition, as laid out by the Iridium Court, the paramount determination in reviewing the

settlement, if this issue exists, is whether the settlement violates some other fundamental principle of the Bankruptcy Code including, as was the case in Iridium, the fair and equitable absolute priority rule.

That does not appear to me to be the case here, so I will look at the other factors in the context of substantive consolidation analysis. It is clear to me that there is a material, legitimate dispute that good lawyers could pursue for a long and expensive time over whether these Debtors should be substantively consolidated or not. Frankly, it does not appear to me that the first of the two Augie/Restivo prongs raises much of an issue.

At least while these Debtors were solvent, the creditors dealt with them on an independent basis, by and large, including Wilmington Trust where there were separate guarantees of the notes for which Wilmington Trust is the Trustee as well as trade creditors who had agreements with specific Debtor entities.

On the other hand, the Debtors had a fundamentally fairly simple cash management system where their receipts were swept on a daily basis into a concentration account, in essence consolidated, and only net balances were maintained so you would have multiple Debtors contributing or borrowing from the concentration account without any easily implemented way to determine which Debtors could, in effect,

be said to be making transfers to which other Debtors and vice versa.

It is clear to me from Mr. Murphy's declaration that tracing those types of transactions between the entities as opposed to a net amount owing to the group would be complex, lengthy, and very expensive, and ultimately fraught with uncertainty.

Even in the two-and-a-half months spent in tracing post-petition transactions on a debtor-by-debtor basis, Mr. Murphy testified credibly that he had only a 80 to 90 percent level of confidence that that tracing was accurate and, of course, that was an expensive and lengthy process just for the slightly under one-year period of this case, although at that time it was, I guess, probably about 10 months or even shorter since I believe it was completed in May.

That problem highlights the very real likelihood that in a fully contested substantive consolidation case, the second prong in the Augie/Restivo analysis, which again, is an independent basis for substantive consolidation, would be found. Again, although that prong is sometimes loosely referred to in briefs and even in some cases as requiring an impossibility of disentangling the corporate affairs, that's not how the Circuit phrases it. Again, it's phrased as the affairs of the Debtors are so entangled, consolidation will

benefit all creditors.

And it is clear that where the Court believes that the cost of conducting such an investigation, reconciliation, and audit will be prohibitive in the context of the case, the Court will approve a reasonable substantive consolidation settlement. See In RE: Republic Airways Holdings, 565 B.R. at 719 and In RE: Winn-Dixie Stores at Page 750 -- I'm sorry, 356 B.R. at Page 250.

Again, the context here is not something that, when the parties dealt with -- when the creditors dealt with these Debtors pre-bankruptcy, they reasonably contemplated, which is that there would be such a thin margin on administrative expense solvency that enforcing intercompany claims debtor by debtor as opposed to simply netting out those claims through the cash management system against an overall solvent business would be meaningful.

It appears to me, therefore, that settling substantive consolidation issues on an assumption that it would be likely on a 75 percent basis that the Court would ultimately direct substantive consolidation is reasonable in light of the Iridium factors pertaining to the costs, risks, and delay of litigation.

The parties negotiating the settlement were clearly fiduciaries for all the Debtors as well as the Debtors unsecured creditors, on the one hand, that is, the

Debtors themselves and the Unsecured Creditors' Committee and the PBGC on the other, the Debtors' largest creditor and also a member of the Creditors' Committee.

I believe not only were the professionals negotiating that substantive consolidation settlement capable and experienced, but actually acting in good faith and respect of all the Debtors including Debtors that could make an argument that they would be unduly harmed by the substantive consolidation.

The plan went out for a vote and generally was accepted, but there are classes of unsecured creditors of certain Debtors that have rejected the plan under Section 1129(a)(8) on the dollar threshold; although, as set forth in the ballot declarations, in terms of numbers of those voting, the majority -- actually, a super majority in each rejecting class -- accepted the plan. So at best, it appears to me that the paramount interests of creditors and their support of the settlement, at best for Wilmington Trust, is neutral.

No other creditor has objected to substantive consolidation; although, of course, Wilmington Trust is speaking as an indentured Trustee for a group of creditors, some of whom, however, are very well-heeled and have not made their own separate objection. And the creditors in the rejecting classes in terms of numbers of those voting,

again, have by a large majority accepted the plan which was a factor that the Winn-Dixie Stores opinion took into account as a positive, 356 B.R. at 249 through 250.

As I noted, substantive consolidation being an equitable remedy and a flexible concept, the Court has the power to approve adjustments to substantive consolidation that would relieve those who would otherwise be unduly prejudiced by the consolidation of, at least, the undue amount of the prejudice. That is the case under this plan which provides that certain holders of claims at estates that appear to be more solvent than others will have a bump-up in their recovery.

That chart is laid out in the Debtors' reply memorandum as well as Mr. Murphy's declaration. As a percentage matter, the bump-up is meaningful and I believe when taking into account the relatively modest recoveries of all unsecured creditors that are projected and the benefits of the interlinked PBGC settlement, particularly the KCD resolution which would, if not approved, substantially reduce down to nearly nothing the recoveries by the bump-up creditors against their then deconsolidated, more solvent Debtors.

The bump-up is sufficient to adequately protect creditors that have multiple sources of recovery that would have those sources eliminated or reduced to one under a

strict substantive consolidation plan. Again, the alternative would be, I believe, a necessity to open up confirmation for individual Debtors on a debtor-by-debtor basis which then would require as part of the 1129(a)(9) and 1129(a)(11) feasibility analyses to do an analysis on a debtor-by-debtor basis of intercompany claims.

And by intercompany claims, I don't mean claims against the common pot through the consolidation account, but rather a debtor-by-debtor, transfer-by-transfer analysis. I believe that would be prohibitively expensive based on the facts before me and the Debtors' current cash positions on a debtor-by-debtor basis.

As far as the prohibitively expensive aspect of it, there is no dollar estimate of what it would cost, but I do accept as credible Mr. Murphy's testimony that based on the two-and-a-half months' effort to do such an analysis with respect to the post-petition period, to do a comprehensive analysis on the prepetition period would be extremely expensive, and prohibitively so given the Debtors' cash position.

It would, to my mind, simply lead to another settlement after all of the estate's assets would be reduced and the KCD claim laid on top of the Debtors' balance sheets, which would benefit no one. Given the ultimate flexibility that I have based on an across the board benefit

analysis, it appears to me, therefore, under the caselaw that the substantive consolidation/PBGC settlement is warranted here, so I will deny Wilmington Trust's objection on that basis.

Wilmington Trust also objected on the grounds that separately classifying the PBGC violated Section 1122 and 1123 of the Bankruptcy Code and/or arguably meant that the plan was not being pursued in good faith under Section 1129(a)(3). I find, to the contrary, that given PBGC's unusual rights against the Debtors and its power with respect to KCD, it was entirely reasonable and appropriate to classify it separately. Lumping it in with other unsecured creditors would've, in fact, skewed those classes.

Indeed, it appears to me, given the size of PBGC's claims, it may have well results in the rejecting classes voting in favor of -- being deemed to have voted in favor of the plan in certain of the Debtor entities, which wouldn't have been right anyway, given PBGC's unique position in the case, including its rights, explicit and implicit, with respect to KCD. Given that it was properly classified, the 1129(a)(3) objection would not fly, either.

Finally, Wilmington Trust objects to a provision in the plan which is somewhat differently worded in the liquidation trust agreement regarding the payment of its reasonable fees and expenses. Frankly, to my mind, there is

some confusion on how those provisions work. It is clear to me, however, that both sides agree that Wilmington can be limited to its charging lien and that the Debtors' estates do not have to separately in a legal manner pay its fees and expenses.

I think the confirmation order should be made clear that under the plan, the Debtors' estates will pay Wilmington Trust's legal fees and expenses regardless of whether it opposes any action that the Debtors take, but that such payment shall be only in the discretion of the Debtors and the Debtors can limit such payment to the ordinary and customary work that an indentured Trustee does outside of a bankruptcy case, including in facilitating distributions and answering questions.

The reason for that limitation is that I think it is -- there should be no question that an indentured Trustee should feel free to raise any legitimate objection or make any legitimate statement in support of an action by a Debtor in bankruptcy and should not be forced to decide whether to do so based on whether its fees will be paid or not by the Debtors' estate.

Okay. So I think we have, then, Cyrus.

MR. KRELLER: Good afternoon, Your Honor. Thomas Kreller of Millbank, LLP on behalf of Cyrus Capital Partners.

THE COURT: Afternoon.

MR. KRELLER: Your Honor, just for -- just as a reminder, Cyrus is the holder of unsecured claims in the approximate amount -- in something like $600 million against various Debtors. By virtue of those claims, I believe Cyrus is next to PBGC, the biggest unsecured creditor in these cases. We also have a disputed 507(b) claim, disputed and under appeal from your ruling disallowing that claim.

Your Honor, I'll be relatively brief, recognizing that at least most of the horse just left the barn. We --

THE COURT: Well, again, you -- I asked you. You're not -- you didn't deal with substantive consolidation, so you're -- I haven't dealt with your issues yet.

MR. KRELLER: I understand that, Your Honor.

THE COURT: Okay.

MR. KRELLER: But clearly, the approval of those settlements, it leads a long way towards confirmation.

THE COURT: Right.

MR. KRELLER: That's my only point.

THE COURT: Okay.

MR. KRELLER: And so I'm not going to belabor those particular arguments. I do want to state, for the record, our objections still stand, and notwithstanding our attempting to work with the Debtors and others on language

in the confirmation order that are under discussion, some points I'll talk about, our doing so doesn't constitute a withdrawal of our objection. Our objections still stand, Your Honor. We don't believe this plan should be confirmed. We think the estates are hopelessly administratively insolvent and likely will be at least for a very long time.

The plan -- this plan is not the simple waterfall plan that Mr. Schrock has been touting for months now. It has become a bit of a Frankenstein monster with various funds being diverted in various directions that are not necessarily consistent with a simple waterfall plan. And, Your Honor, I'd note, obviously already you've approved the PBGC settlement and the substantive consolidation settlement, so I won't get into the how the effects of those, a bit of a shell game going there on some of that stuff, but the other --

THE COURT: Well, if it's a shell game, you should've raised the issues. I'm going to say it again. Do you really want to go over it? I mean, do you have new facts to raise on those issues?

MR. KRELLER: No, I don't, Your Honor.

THE COURT: So what's the -- so how is it a shell game?

MR. KRELLER: Your Honor, the other piece of the diversion of funds is the $25 million that's going out to

essentially serve as a retainer for the Committee professionals and that UCC settlement as well is a bit suspect because all that was really resolved there was which law firm was going to represent the Trust in the litigation and --

THE COURT: It's not a big settlement as far as I'm concerned, although it's important to get done. I agree with that.

MR. KRELLER: Well, Your Honor, well -- I want to talk about the $25 million in a minute. It's not a big settlement. It certainly doesn't appear to have had any benefit for the creditors or their recovery. The beneficiary of that settlement appears to be Akin Gump.

THE COURT: Wait, the $25 million or --

MR. KRELLER: Yes.

THE COURT: -- so, you stated -- is that even in your objection? I don't think you raised that in your objection.

MR. KRELLER: I don't know that I did, Your Honor.

THE COURT: No, you didn't.

MR. KRELLER: But the --

THE COURT: So what is the point? I mean, you're saying that the Debtors should not have a litigation fund to pursue their complaint?

MR. KRELLER: I'm not saying that, Your Honor.

I'm saying --

THE COURT: Okay.

MR. KRELLER: -- that those funds coming out of the estate ahead of potentially administrative claimants isn't appropriate and I would question the magnitude of that fund given the fact that the work has already been done and paid for twice by the estates to both the UCC's investigation and the special committee of the board's investigation.

But, Your Honor, I'm not standing her to belabor any of these points.

THE COURT: Well, good, because they're not in your objection.

MR. KRELLER: You have your record. You've made the assessment. Apparently, the Debtors have cleared the lowest rung on the range of reasonableness and so I'll move on, Your Honor. The point that I really want to address is kind of the metaphysical question that you were dealing with a bit on Thursday and less so today which is, what happens when you have a confirmed plan that may not go effective for a prolonged period of time, and I think that's the upshot of even the Debtors' own testimony on there.

I don't believe any of their witnesses could give you any real sense of how long it would be before there would actually be funds sufficient to pay the administrative

claims, so Your Honor, my view is it's probably closer to three years than three months, but that will be what it will be.

The issue of a confirmed but not yet effective plan, though, Your Honor, gives rise to a handful of issues and these really come up in the proposed confirmation order and we've been discussing these with Debtors' counsel and we have -- I think we've had agreement on a couple and we still have some outstanding, but I think they're important. Your Honor, when the plan is confirmed but not yet effective, nothing really changes in terms of the Debtor. The Debtor is a Debtor in Possession. The plan is not actionable or implementable and the parties simply wait in the status quo, waiting for the effective date.

That leaves the Debtors remaining as Debtors in Possession. It leaves the UCC in place with its rights and duties and the case, essentially, proceeds as it is with ordinary course transactions being permitted under the code, but anything outside the ordinary course or any extraordinary creditor distributions to await the effective date of the plan.

That structure, that confirm and wait for effective date the Debtors have proposed conceptually works and occurs in other cases, but the notion there is that essentially the money doesn't start moving until the

effective date occurs because you don't have an effective plan. Now, in the administrative expense settlement that got announced earlier last week, there's -- that created this wrinkle where the Debtors actually start to move money.

They start to fund $20 million into the litigation to be earmarked, to be segregated into the litigation trust or into litigation activities. Your Honor, we don't believe the segregation is appropriate or necessary, but if those words are going to be used, we think it ought to be clear that they are without prejudice to the rights of any of the creditors to pursue those funds as assets of the estate.

THE COURT: Okay.

MR. KRELLER: The --

THE COURT: I thought the proposed order actually made it clear that this was estate -- this continued to be estate property, it was not property held in trust or anything like that.

MR. KRELLER: Well, it doesn't go quite that far. It does say it's estate property.

THE COURT: Right.

MR. KRELLER: But the very notion that it's somehow being segregated or that segregation is appropriate leads to the implication that somehow rights are being affected. And, Your Honor, in our view --

THE COURT: It's $15 million, right? It's not --

MR. KRELLER: It's -- I believe it's $20 million. It's 15 and then 5 coming out of one of the -- out of the winddown account.

THE COURT: Right. Okay.

MR. KRELLER: And then that's subject to top up from first assets in to get it up to 25.

THE COURT: Right. Okay.

MR. KRELLER: So certainly, the implication is that those funds are being set aside, segregated, ear marked, which sounds to me -- and I don't see anything in the documents that gives me great comfort otherwise -- that they're being removed one step further away from creditors and potential creditor distributions than other assets or cash the estates may have.

And, Your Honor, I would submit that during the post-confirmation, pre-effective date period, there's no reason for that money to move and there's no reason for creditors' rights to be impaired or potentially impaired by virtue of the segregation of those funds. The professionals will remain. They'll be doing the work they do. The estate professionals will be subject to ordinary course fee procedures in these cases and they'll have access to the carveout and the other accounts that they have for their benefit.

There's no reason to move this money. They'll do

the work. They'll do whatever they're doing in the litigation at the direction of the litigation designees, but somehow setting this money aside to the potential prejudice of creditors is a problem and it's premature. That money was always going to be funded under the plan on the effective date, but somehow this provision pulling it forward to the confirmation order found its way into the administrative claims settlement, an issue that appears to be completely unrelated but nonetheless is significant.

We've proposed language and there's some language going back and forth to try to make clear and amplify and extend upon the Debtors' draft language about the funds being estate funds, but we don't have agreement there yet, Your Honor, and that language ought to be protective of creditors and it ought to make clear that those funds, whether they're in the estate as estate funds or whether the plan goes effective and those funds go into the litigation trust, that they are litigation trust assets that are subject to the claims and rights of creditors to creditor distributions.

That money ought to be available to creditors, if it hasn't been expended.

THE COURT: So what is the language you're proposing?

MR. KRELLER: Your Honor, I can -- well, we don't

have agreement on the language and there's, I guess, a couple of different sets of language going back and forth. I had proposed language last -- earlier this morning to the Debtors which they rejected and ESL's counsel had proposed language to that effect that's been circulating during the hearing and that's been rejected as well.

Your Honor, I'll look for -- if you give me a moment, I'll look for my... The language, Your Honor, and this is language that ESL and Cyrus would live with, and that language is, "for the avoidance of doubt and notwithstanding anything to the contrary contained in the plan or the liquidating trust agreement, in the event that any disputed claim ultimately becomes an allowed claim," -- and it's defined as a subsequently allowed claim -- "including by reason of any appeals of any orders of this Court disallowing such claim, nothing in the confirmation order, plan, or the liquidating trust agreement limits the ability of the holder of any such subsequently allowed claim to assert a claim including a priority claim or to obtain a recovery from any liquidating trust assets to satisfy such subsequently allowed claim including, without limitation, the funds in the litigation funding --

THE COURT: That's quite different than what you were just talking to me about. That's basically saying that even after -- the liquidating trust doesn't go into

existence until the plan actually goes effective.

MR. KRELLER: Correct.

THE COURT: So that doesn't work. I can see why they rejected that.

MR. KRELLER: Well, Your Honor, it's at both points in time, though.

THE COURT: No.

MR. KRELLER: The liquidating trust assets are defined as the assets that in the liquidating trust and available for distributions to creditors.

THE COURT: I think you're going to have to divide up the two. I mean, there's a fundamental issue that was raised in your objection, was that you wanted a reserve for the claim that I had already ruled on. To me, that seemed to be contrary to the caselaw and flipping the whole notion of who should be posting a bond for a stay pending appeal.

But I thought you were going on a very different tack here, which is that pending the effective date, the money is property of the estate and is not being held in trust or otherwise. I mean --

MR. KRELLER: And that's --

THE COURT: I have no problem with that. It's not being held in trust, right?

MR. SCHROCK: Your Honor, we have language in the confirmation order that says that. It's Paragraph 57.

THE COURT: Well, does it say it's not being held in trust?

MR. SCHROCK: Yeah, Your Honor, I'll just read it. It says, "For the avoidance of doubt, the funds in the litigation funding account and the cash reserve account shall remain property of the estates and after the effective date, liquidating trust assets provided that use of such funds shall be subject to plan and/or liquidating trust agreement and the funds in the cash reserve account shall be subject to the administrative expense claims consent program."

THE COURT: Okay. So, look, if -- dealing with the post-effective date aspect of this, I think you all should just stay away from. I mean, that all -- it's all wrapped up in issues of mootness and appeal and all those sorts of things. Seeking a stay, which hasn't been sought because there's nothing to seek a stay of because the plan hasn't been confirmed. I think you should just focus on the pre-effective date period.

And I mean, as long as it's clear that this money is property of the estate and not being held in trust...

MR. KRELLER: Your Honor, it ought not be held in trust in the post-effective date period. I --

THE COURT: Well, if the plan provides for that level of funding, it's not held in trust but that's what the

plan would provide for.

MR. KRELLER: The cash will, to the extent it's not been consumed, that cash will be a liquidating trust asset that ought --

THE COURT: Right.

MR. KRELLER: -- to be available to creditors.

THE COURT: If the plan says to the contrary, and literally no one has objected on that basis, I don't see why -- except for ESL, the target of the litigation. You know --

MR. KRELLER: The --

THE COURT: -- I guess the answer is, tough. The plan controls. I --

MR. KRELLER: Well, Your Honor, this issue came about because of how this provision found its way into the administrative expense settlement. And so the notion that no one objected to it, the money was always going to be an effective date issue; otherwise, everything was staying in the estate. And all we're looking for in terms of the post-effective date period is clarification that there's no intention that the liquidating trust assets including those funds would somehow be withheld from creditors with allowed claims.

THE COURT: Well --

MR. KRELLER: If it gets used up, it gets used up

and it's not there. But if it is there and creditors including administrative creditors, have claims assertible against that money, they should have that right to be able to pursue those funds and not --

THE COURT: Well --

MR. KRELLER: -- have the professionals play keep-away with them.

THE COURT: But it's -- the money is being -- well, when you say used up, what do you mean? I mean, obviously --

MR. KRELLER: Spent on --

THE COURT: It will be --

MR. KRELLER: Spend on professionals.

THE COURT: If it's not spent on professionals, then yes, it goes over to the general uses, but I guess I...

MR. KRELLER: Your Honor, I'm actually surprised this is controversial with the Debtors and the UCC.

THE COURT: It's controversial for the post-effective date period and I understand their position entirely on that point. As far as the pre-effective date period is concerned, saying that it's property of the estate and not being held in trust is enough. You don't need to specify who has a right to it under what circumstances. Everyone would have a right to it, pre-bankruptcy, if there's circumstances that would give you a right to it.

MR. KRELLER: I --

THE COURT: I mean, pre-effective date.

MR. KRELLER: That's my position, Your Honor, which is why I don't understand the --

THE COURT: Well, the language you read me also covered the post-effective date.

MR. KRELLER: It does, but --

THE COURT: Well, but it shouldn't.

MR. KRELLER: What is the purpose of the segregation if, in fact, they remain estate assets --

THE COURT: Because you want to keep track of it.

MR. KRELLER: -- subject to creditor claims?

THE COURT: You want to know where it is. You know what? It's psychological, frankly. That's what it is. And I think who is objecting -- I think the people who are objecting to this are experiencing the psychological effect which, I think, was intended. That's why litigation budgets are largely created, just for that reason.

MR. KRELLER: Your Honor --

THE COURT: So I don't --

MR. KRELLER: Your Honor, as the second largest unsecured creditors in the case and potentially with a 507, we stand to benefit probably more than most from successful -- from the successes of the litigation trust.

THE COURT: Well, you're also --

MR. KRELLER: So --

THE COURT: -- an investor in Transform and could be -- that investment could be hurt by adverse litigation against Transform's controlling party, so look. It's fine that you're a large creditor. I get that. But I don't see anyone else complaining about this language. It just doesn't -- it's property of the estate. It's there, yes. Everyone knows that it's intended to be used post-effective date to litigate with.

And if the rulings against your clients are reversed or if I confirm the plan, the plan confirmation order is reversed, we'll be in a different environment. But that presumes all sort of things that I can't deal with at this point, including your burden to get a stay of various orders and maybe have to post a bond and all those sorts of things. I think you're basically trying to get the bond flipped on its head here by having the debtor, in essence, post the bond.

At least that's what the objection was all about and I'm setting up a reserve. It just doesn't --

MR. KRELLER: Well --

THE COURT: Doesn't compute.

MR. KRELLER: Your Honor, I'll -- on this point, the reason that nobody else has objected to this is because this showed up at midnight in a Tuesday night filing last

week that --

THE COURT: Well --

MR. KRELLER: That was the first point in time in which any money was going to move --

THE COURT: But it's not moving.

MR. KRELLER: -- pre-effective date

THE COURT: It's not moving. It's clear that it's property of the estate, not being held in trust. It's under this rubric because everyone knows that's what this is intended to do ultimately when the plan goes effective and it was part of the negotiation of the administrative claims settlement procedures for the party to know where the money was going to be ultimately. But it's not -- it's psychological. It has no legal consequences.

MR. KRELLER: Your Honor, with that statement from you that it -- that the segregation has no legal consequences --

THE COURT: Pre-effective.

MR. KRELLER: -- I'll stop talking about --

THE COURT: Okay. Pre-effective.

MR. KRELLER: -- that issue.

THE COURT: Okay.

MR. KRELLER: On the reserve issue, the plan provides that disputed claims reserves shall be provided on the effective date for disputed claims. The 507(b) claims

are disputed claims because they are not the subject of a final order. The plain reading, the words of the plan, are what would entitle us to a reserve.

THE COURT: There's not --

MR. KRELLER: And now, Your Honor, I don't think that's --

THE COURT: There's no stay of my order.

MR. KRELLER: There is no stay of your order, but it is not a final order.

THE COURT: I --

MR. KRELLER: But, Your Honor, that's not for today, either. That only becomes relevant if there is an effective date coming where there's actually money to deal with and the appeal might be in a different -- those --

THE COURT: It may well be --

MR. KRELLER: -- claims might be in a different status --

THE COURT: But I'm certainly not --

MR. KRELLER: -- at that point in time.

THE COURT: I'm not setting a reserve at this point.

MR. KRELLER: I'm not asking you to, Your Honor.

THE COURT: Okay.

MR. KRELLER: I interpret the plan as it's written.

THE COURT: Okay. I'm not sure whether a reserve is required at any point, but I think at this point, it's not appropriate to order one and it does seem to me that Judge Farnan is right on here in In RE: Oakwood Homes Corp., 329 B.R. 19.

MR. KRELLER: Your Honor, I think the facts of that case were a bit different. I think that that claim, the request for a disputed claims reserve was actually denied in those cases. I think there was a different procedural posture. It wasn't just simply a disputed claim for plan purposes. But again, Your Honor, that's not -- that's actually not a confirmation issue for today. It's an effective date issue for the flow of funds, what the flow of funds looks like in the event that there are funds to flow.

THE COURT: Okay.

MR. KRELLER: Your Honor, a couple of other points. I had simply -- I had requested of the Debtors a fairly simple sentence or two basically stating that in the confirmation order that pending the plan effective date, Debtors remain as Debtors in Possession with all of their rights and obligations and subject to the requirements of the Bankruptcy Code and the Bankruptcy Rules and other applicable law, while in the estates and while as Debtors in Possession.

That language was rejected out of hand. I don't

quite understand that. It appears to be that that is, I think the reality and that's what I hear you saying as well.

THE COURT: Right.

MR. KRELLER: And, Your Honor, I --

THE COURT: I mean, that's the law.

MR. KRELLER: It is, Your Honor, but in a case where these Debtors may be operating as Debtors in Possession for a long time before a plan ever goes effective, it would seem to me that a simple statement in the confirmation order --

THE COURT: We don't need that. I mean, then (indiscernible) start incorporating specific provisions of the bankruptcy code and it's just --

MR. KRELLER: The language --

THE COURT: The law is clear on this point.

MR. KRELLER: That's fine, Your Honor. We had also asked, there's a provision and it's been beefed up in the order for advance notice of the anticipated occurrence of the effective date.

THE COURT: Right.

MR. KRELLER: Twenty days' notice with a 10-day period to -- for parties to object if they have issues with that.

THE COURT: Right.

MR. KRELLER: We had proposed that a similar

notice provision go in with respect to post-effective date --

THE COURT: That's --

MR. KRELLER: -- future distributions.

THE COURT: And I asked Mr. Singh that. I think that's in there now, you said?

MR. SCHROCK: We put in the 20 days, Your Honor.

THE COURT: For each distribution?

MR. SCHROCK: Yes, Your Honor.

THE COURT: Okay.

MR. SCHROCK: Well, we didn't put in, you know, the rights to object and the like.

THE COURT: Just the notice?

MR. SCHROCK: Just the notice.

THE COURT: In 20 days.

MR. SCHROCK: Correct.

MR. SINGH: Your Honor, there's actually a 30-day provision already in the plan and the trust agreement.

THE COURT: Okay. I don't think there should be --

MR. SINGH: For future --

THE COURT: -- any implications that you can't come in and say, they're making payments that they shouldn't be making or whatever.

MR. KRELLER: I'll accept that, Your Honor. I

have not --

THE COURT: I mean, there's only one reason to give notice, which is someone complains.

MR. DUBLIN: It's in the definition of distribution. It says 30 days' advance notice.

MR. KRELLER: Okay.

MR. DUBLIN: You get an extra 10.

MR. KRELLER: Your Honor, the confirmation order in various places contains provision approving things like the plan supplement documents and finding those and approving those documents. I had suggested language that simply said those -- only those documents that are in existence and on file as of the date of the confirmation order are you approving. And again --

THE COURT: I can't approve something I haven't seen.

MR. KRELLER: Well, Your Honor, that -- that seemed to be the case to me as well, but I do think, again, given the potentially prolonged lag, I think that would be a clarification that would be worth having.

THE COURT: Well, I mean, there -- this wasn't a provision I focused on, but I'm assuming the plan supplement and related documents are defined in a way so it's not including documents that would be submitted in the future unless they're amendments that don't have any material

adverse effect on anybody.

MR. KRELLER: I don't know whether they are or not, Your Honor.

THE COURT: No --

MR. KRELLER: But there's -- you have a long --

THE COURT: That's how it should be.

MR. KRELLER: You have a long period of time with --

THE COURT: I know, but --

MR. KRELLER: -- with potentially --

THE COURT: I'm not going to approve anything I haven't seen.

MR. KRELLER: I understand, Your Honor.

THE COURT: Okay.

MR. KRELLER: Nor should you be asked to, but that's --

THE COURT: All right.

MR. KRELLER: -- the way the language reads --

MR. SINGH: Your Honor, can assure you, we're not --

THE COURT: Well, when I go through it, I'll -- if there's an issue there, I'll strike that out.

MR. KRELLER: Thank you, Your Honor.

THE COURT: Okay.

MR. KRELLER: And then, Your Honor, I would just

note in Paragraph 24, I believe, of the draft order, there's actually a provision that allows the Debtors to be -- and this, again, is in our limbo pre-effective date period -- that would allow the Debtors to be paying litigation professionals subject to monthly invoices and it looks to be something that -- again, I think this is just inadvertence -- because we're still in the cases at that point in time, those professionals should just be getting paid under the existing fee --

THE COURT: Under the fee order.

MR. KRELLER: Under the fee order.

THE COURT: Right.

MR. KRELLER: And there's no reason that that would -- should change on confirmation --

THE COURT: Okay.

MR. KRELLER: -- of the plan.

THE COURT: No, that's fine. Again, it's not a limbo period. It's, as you said, the Debtor is the Debtor in Possession and this litigation committee has been created to deal with the committee -- I mean, deal with the litigation. Similarly, there's the reporting mechanism on the claims settlement, but those are things that I'm approving.

MR. SINGH: To the extent it was unclear, we so stipulate.

THE COURT: Okay. All right.

MR. KRELLER: That's all I have --

THE COURT: Okay.

MR. KRELLER: -- Your Honor. Thank you.

THE COURT: And we've confirmed that Cyrus is not a releasing party, right?

MR. KRELLER: Right, Your Honor.

THE COURT: Okay.

MR. KRELLER: Correct, Your Honor.

THE COURT: Okay. So, I mean, are there -- I don't think there are any other objections in your objection. Is there something that is raised that I should address?

MR. KRELLER: No, Your Honor. I believe we covered it all.

THE COURT: Okay. All right, thanks.

MR. MOLONEY: Good afternoon, Your Honor. Tom Moloney on behalf ESL.

THE COURT: Afternoon.

MR. MOLONEY: Your Honor, we filed two objections. The first one related to the plan and I think that was, essentially, worked out so the plan actually doesn't really prejudice the ability of a subsequently allowed creditor to participate fully. We filed the second objection when saw the plan supplement and I think Your Honor is right. There

are two points in time that are relevant.

There's a point in time when we're still basically in the same status that we are now which is a Debtor in Possession status and as to that point in time, I think Your Honor's statement that they've created an account but it doesn't -- just a nominal account and it has no trust significant, if Paragraph 57 of their order said that, we wouldn't be objecting. It doesn't say that. It says it shall be property of the estate subject to this liquidating trust agreement which had provisions which include not only a single --

THE COURT: But that's subject -- that doesn't go into effect until confirmation.

MR. MOLONEY: I don't know what --

THE COURT: I mean, I'm sorry, the effective date.

MR. MOLONEY: I don't know what that means for -- then for it to be part of the order, though, at this point --

THE COURT: Well, it's a confirmation order, so when it goes effective, the liquidation trust goes effective. Before that, it's not.

MR. MOLONEY: Okay, so then I'll just go to the second part of the argument, what happens then.

THE COURT: Okay.

MR. MOLONEY: But for point of clarity, then,

because I think that it's a mistake to walk away from this podium, I think, without having perfect clarity --

THE COURT: Okay.

MR. MOLONEY: For a point of clarity, unless and until they actually confirm a plan, whatever money they put into --

THE COURT: Unless and until it goes effective.

MR. MOLONEY: It goes effective, until -- have an effective plan, whatever they want to call this account they're setting up, it remains property of the estate and remains subject to the rights of potentially secured creditors and potentially priority creditors who have a higher priority than administrative -- (indiscernible) administrative claims. So now we go to future (indiscernible). Your Honor, admittedly, this is a place holder point.

It's not for -- and we did not seek a reserve and we're not asking you to stay anything. But this is a liquidating plan. Under the code, 1145, they are not entitled to a discharge so they can't get a de facto discharge of our priority claim by playing some game through a trust agreement. So once they're in this future world, if we do, in that future world, prevail and Your Honor, I understand that they don't think we'll prevail. Probably Your Honor doesn't think we'll prevail.

But, you know, I'm always an optimist and so I think there's a chance we'll prevail. And we come back down here and we say, well, Judge, we actually have a secured claim. We can trace our proceeds to this account. Or, Judge, we have a super priority claim and we have higher priority than whatever other use they want to use the money in this account. I don't think at that point in time they can say, well, sorry, if the liquidating trust wants to use that money, so for you to fund a lawsuit against yourself, they should be allowed to do that.

I don't think the plan can provide for that outcome. I don't think it legally can provide for that outcome.

THE COURT: Well, I guess certainly if the plan were confirmed, you would have to get two reversals, right? You'd have to reverse the claims order and confirmation. But you're saying it shouldn't be confirmed in the first place?

MR. MOLONEY: No, I'm not, Your Honor. All -- what I'm saying is, I don't need -- I don't think I need to challenge this plan in any respect. I think the plan as drafted is fine and I don't think I -- I can pursue my appeal. I (indiscernible) claim. I can come back and live in the regime that exists post-confirmation of a liquidating pot plan. This is not a case where, Your Honor, there's a

new business and it needs to have a clean balance sheet --

THE COURT: No, but this is --

MR. MOLONEY: -- and it can't have contingent liabilities.

THE COURT: Look, I think it's -- I ruled on this issue on the U.S. Trustee's objection. I don't believe that the -- I guess you're saying the plan injunction is, effectively, a discharge?

MR. MOLONEY: No, I'm not arguing that.

THE COURT: You're not.

MR. MOLONEY: I'm saying it's just a supplement that they put out. It's only -- it's not the plan at all. I don't have a problem with the plan at all. The plan supplement, which they now incorporate into this order, purports to give to this litigation trust board discretion to set aside on an evergreen basis $25 million or more into an account which no one can get a hold of but them.

THE COURT: But if -- so then the issue is, I think, a fairly technical one.

MR. MOLONEY: Right.

THE COURT: Which is, I think -- I'll go back to what I said earlier. I think you would need to have the reversal of two orders.

MR. MOLONEY: No.

THE COURT: You would have to have the reversal of

the -- well, depends on the timing. But let's say that the plan went effective before there was a determination on the appeal on the 507(b) issue.

MR. MOLONEY: Right.

THE COURT: The plan -- if the plan did go effective, then.

MR. MOLONEY: I don't see why we need any reversals, Your Honor. We just --

THE COURT: Well --

MR. MOLONEY: -- come right back down and assert our claim, if it's allowed.

THE COURT: I'm not sure of that. I think you might need a reversal of the plan, too, of the confirmation order.

MR. MOLONEY: Not if I'm successful right now. Not if I'm successful --

THE COURT: well, but you just said you don't --

MR. MOLONEY: -- right now in getting Your Honor --

THE COURT: But you just said you don't mind if the plan is confirmed.

MR. MOLONEY: Correct. It's just the plan supplement provision.

THE COURT: But that's --

MR. MOLONEY: If the plan supplement provision is

consistent with the plan, I don't have a problem with the plan. The plan supplement provision, what is says, Your Honor, in the plan supplement, it says the litigation board has the right to create a $25 million entitlement or such ever amount as they want, whatever they want. And that -- I want to be clear, if that happens and it's just these three guys --

THE COURT: But the --

MR. MOLONEY: -- sitting there decided that they don't want to pay a particular creditor and they'd rather have the money available to pursue a pipe dream litigation, then I don't think I should have to pay for it.

THE COURT: But the plan itself contemplated funding of the litigation trust.

MR. MOLONEY: I have no problem with that, Your Honor.

THE COURT: So what's the distinction?

MR. MOLONEY: The distinction is that the money that's available depends on what's the money that's available. They just cannot cut off the rights -- the plan doesn't create money, right? The plan doesn't create assets. The plan just says, whatever money is here is for use in these purposes. And so if there is no money to fund this trust, that's not my problem, all due respect.

And certainly if I have a super priority claim and

I say, you're going to have to pay me before you -- you can go ahead and fund the trust. You can go out and get -- find litigation funding or you can go out and find a contingency lawyer to do this because there's no way that if this was a viable claim it couldn't be funded a million ways other than stealing my money.

THE COURT: Is this in your supplemental objection?

MR. MOLONEY: Yes, Your Honor.

THE COURT: Where?

MR. MOLONEY: Exactly.

THE COURT: I don't --

MR. MOLONEY: This is exactly the part. We made this so we wanted clarity that these funds -- Paragraph 6. "ESL, of course, recognizes it will have no right to payment unless it prevails on appeal, but should ESL prevail, its ability to collect on traceable collateral proceeds or to assert a 507(b) statutory priority claim cannot lawfully be compromised by these self-help measures in the plan trust agreement." That's our position.

And this is not -- there's nothing in the Bankruptcy Code that authorizes you to do this. They're not held in the discharge. There's nothing in the Bankruptcy Code that says --

THE COURT: But this doesn't have anything to do

with the discharge.

MR. MOLONEY: Effectively, it's a billed -- pertained to discharge because it's aimed at one group of creditors. It's to say, look, if they don't want to pay you, they have a right sitting there in the liquidated trust not to pay you. Even though you have a priority claim and you've won an appeal and the Bankruptcy Code says you should be paid ahead of everybody else, if they don't want to do it, they don't have to.

THE COURT: The only thing I'm grappling with is, again, if you just appeal the -- well, if you just have the appeal that's currently on file.

MR. MOLONEY: Correct.

THE COURT: And you don't appeal confirmation, then there's a -- or you do appeal confirmation, there's all separate standard for dealing with that type of appeal --

MR. MOLONEY: Yeah, but I don't see --

THE COURT: -- that deals with mootness and those sorts of --

MR. MOLONEY: Yeah. I don't see why I have to be involved in that at all. I really have no interest in it.

THE COURT: Because it's the plan.

MR. MOLONEY: But the plan doesn't -- with all due respect, Your Honor. I'm fine with the plan. This is a trust supplement agreement filed at 2:00 in the morning the

day before a hearing that contains other provisions that are not in the plan.

THE COURT: Well, we should look at -- we should at the disclosure too. What does the disclosure statement say on the funding of the plan?

MR. SINGH: Your Honor, I believe it -- you know, we'll get the specific page reference. But I know it references the liquid- -- you know, the liquidating trust with approximately $25 million in it for --

THE COURT: Yeah. I mean, the settlement that came out recently cut back on that.

MR. SINGH: Right.

THE COURT: Didn't add to it.

MR. SINGH: Right.

MR. MOLONEY: But the language in the trust agreement makes it evergreen, Your Honor. There's nothing in that disclosure statement that says they can do it on an evergreen basis.

MR. SINGH: This seems like an equitable move.

MR. MOLONEY: It's not an equitable move.

THE COURT: I understand if you're modifying the plan, including how it's described in the disclosure statement. You certainly can describe generally in the disclosure statement documents that are filed later, if they're consistent with that, then that's what I would be

confirming. So maybe it's the evergreen feature. I don't, you know -- I think they contemplated 20 million -- I think it's --

MR. MOLONEY: As a practical matter, $25 million is probably going to be spent before I ever can get back down here, so I'm really more concerned with the evergreen.

THE COURT: Well, I doubt that. I doubt it would be all spent, although when litigators, as I say, breathe on a file, it's $50,000. I'm looking for the disclosure statement reference to this at this point. I think it's --

MR. SINGH: Your Honor, first of all, I don't think it's an evergreen. I think it's a one-time funding.

THE COURT: Okay.

MR. MOLONEY: It's what it says.

MR. SINGH: Oh, Your Honor, it's in Page -- excuse me -- it's Page 3 of the disclosure statement where we talk about the litigation assets. So I'll read the two sentences: "Upon the transfer of the liquidating trust assets, the Debtors shall have no interest in or with respect to the liquidating trust assets or liquidating trust. The Debtors estimate that the liquidating trust will be funded with approximately $25 million on the effective date," which relates to this issue of segregation, which we disclosed.

MR. MOLONEY: Okay. That makes my point for me,

Your Honor. But before I get there, if I --

THE COURT: But why? That's the plan that -- I mean, why is that -- look, again --

MR. MOLONEY: It doesn't say a word about it being segregated from other creditors. It doesn't say --

THE COURT: No, but it'll be transferred to the trust, so that's --

MR. MOLONEY: The trust is for the benefit of the creditors, right, not for the benefit -- I thought it was for the benefit of the creditors, not for the benefit of the three trustees and professionals.

THE COURT: No, but it says it's funded with the -- can you read the sentence again, Mr. Singh?

MR. SINGH: Yes. Again, Page 3: "Debtors estimate that the liquidating trust will be funded with approximately $25 million on the effective date."

THE COURT: Okay. All right.

MR. MOLONEY: If they have the money and there's no prior claim to it, they can fund it; I have no problem with that.

THE COURT: Okay.

MR. MOLONEY: But if they don't -- but if we have a prior claim, we should be able to object to that, and we shouldn't have to object to the plan.

THE COURT: No. I think you should -- I think you

do have to seek a stay if you're saying that this funding shouldn't happen. I think the $25 million is clearly for litigation purposes, right? It's not for distribution purposes.

MR. SINGH: Absolutely, Your Honor. And if you read the definitions throughout the plan, they make clear that what we are distributing is net proceeds, which allows the directors the discretion every time they go to make a distribution to decide how much they want to hold back for going forward purposes.

THE COURT: Right.

MR. SINGH: I feel like we're being penalized that we actually went out and said well, it'll be $25 million, what everybody's been told.

THE COURT: I agree with you, Mr. Moloney, that if the effective date occurs and subsequently, the 507 is reversed and you have -- you can trace your claim to the funds, et cetera, that you should be able to go after them. But I think you will need, in addition to getting that order reversed, you would have to get either a stay or you'd have to get the confirmation order reversed. Because I think that clear context of this plan is that the funding, subject to, you know, the appeal issues, is for litigation purposes.

MR. MOLONEY: Your Honor, can I just raise an issue then? The document that they actually filed, which

says that --

THE COURT: This is the supplement.

MR. MOLONEY: The supplement, in Paragraph B -- I'm reading from Paragraph B on Page 4, it's 1.3(b). It's what we quoted in our objection. It says that, "In addition to that there should be set outside $25 million, is it provided, however, that the funding may be increased from time to time during the term of litigation trust, from the proceeds of the liquidating trust assets, or from such other sources as may be determined in the sole discretion of the liquidating trust board."

I read that as evergreen language. That, where it says that, "funding may be increased from time to time during the term of the litigation trust, from the proceeds of the liquidating trust assets, or from such other sources as may be determined in the sole discretion of the litigation trust board."

I read that -- I don't read that as being consistent at all with the disclosure of, we may have $25 million. This says that we're going to have a reprise of what happened under the DIP order where they're going to say there's a special account set aside and they're going to put all money in there. And it's going to just frustrate our rights to get paid if we win our appeal, and that will not be right.

THE COURT: But, again, you can -- right now, there's no allowed claim, all right? So if you win on appeal, it depends on whether the plan has been confirmed and gone effective as to whether and how you could get that money back. It's not just based on winning on the appeal necessarily, because if the plan is confirmed and goes effective, it's binding, it's terms are binding.

MR. MOLONEY: Correct. But today is the day when I have a chance to tell Your Honor that I shouldn't have to -- and I have to tell Your Honor because I can't appeal your ruling, with all due respect, unless I make the case today and you disagree, which you're quite entitled to do. But I have to make the case that perhaps that this particular provision is overreaching and I shouldn't have to include this in my appellate brief; the fact that they've created a liquidating trust fund, which they built a wall -- build a wall around.

THE COURT: But your only basis for going after that provision on a legitimate basis is that the money is more properly distributed on account of a claims that I said it can't be distributed on.

MR. MOLONEY: Well, at the moment -- actually I think at the moment --

THE COURT: Right. And so --

MR. MOLONEY: At the moment, our administrative

claimants who also could be prejudiced by these provisions.

THE COURT: But they don't -- they haven't objected. In fact, they negotiated a reduction of the initial funding instead because they want the lawsuit to go ahead against your clients.

MR. MOLONEY: I don't know that that -- I don't know -- I don't know --

THE COURT: And everyone else did too. Every single administrative objector who objected said, we don't want to cut back on the litigation against ESL. So I think --

MR. MOLONEY: I think -- you know, Your Honor, I think you got to take that with a grain of sale, right?

THE COURT: Well, no. I mean, if I'm going to take any grains of salt, it's ESL saying there shouldn't be so much money to sue me with.

MR. MOLONEY: Well, they're not going to get -- they're not --

THE COURT: So, I mean, the only issue is --

MR. MOLONEY: They're not getting more money from their lawsuit, Your Honor, so why would they care?

THE COURT: All right.

MR. MOLONEY: I mean, as you said, they've objected on the administrative claim and they're getting paid a discount on administrative claim and so, they're

done. So what'll -- they don't have a -- they didn't throw in a kicker.

THE COURT: No, no, that's not true. There are plenty of people who are not going to do the settlement and they're going to wait and get their hundred cents.

MR. MOLONEY: Those people have not -- I've not heard from in court saying --

THE COURT: Well, because they're not unhappy with the result. But, again, it's an easy thing on your brief, which says that to get my remedy, we have to reverse this provision of the plan and go after it. It's pretty easy. And I don't, frankly, even see mootness because it's there, it's sitting there.

MR. MOLONEY: Thank you, Your Honor.

THE COURT: So, you know, so if you asked for a stay, you'd have -- you probably wouldn't get one because it wouldn't be moot. You wouldn't have to post a bond; you just go forward.

MR. MOLONEY: Exactly, Your Honor. Thank you.

THE COURT: Okay, all right.

MR. ANKER: Your Honor, Philip Anker, Wilmer Cutler Pickering Hale and Door. We represent ESL in the litigation that will occur. And I apologize first for tag-teaming you.

THE COURT: All right.

MR. ANKER: And I want to say in interest of full disclosure that I want to give an explanation.

THE COURT: Well, I'm sorry, this is the --

MR. ANKER: Fraudulent transfer.

THE COURT: So ESL as defendant.

MR. ANKER: Correct.

THE COURT: As opposed to --

MR. ANKER: We represent ESL, Mr. Lampert and related entities.

THE COURT: As opposed to Appellant.

MR. ANKER: Pardon me, Your Honor?

THE COURT: As opposed to Appellant.

MR. ANKER: Correct, Your Honor.

THE COURT: Okay.

MR. ANKER: We're also on the appeal brief. But, yes, Your Honor. I'm here in a different capacity.

THE COURT: Okay.

MR. ANKER: And I want to raise an issue, to be candid, it's not in any objection, but it arises out of the revised administrative claim notice filed this morning.

THE COURT: Right.

MR. ANKER: I didn't see it until I got here at noon.

THE COURT: Okay.

MR. ANKER: And Your Honor obviously was concerned

about disclosure, and my only -- I am rising solely on disclosure.

THE COURT: Okay.

MR. ANKER: In the quote/unquote, "risk factors", the Debtors now say -- and I can point you to the page, but I think you read it today, so I don't think I have to -- that, quote, "The Debtors believe they will receive significant recoveries" end quote, from the proceeds of various litigation, including that against my client.

THE COURT: All right.

MR. ANKER: And that they believe, having done an investigation, that the claims are, quote, "highly meritorious" end quote. And this is obviously a document going out under the imprimatur of a court notice.

THE COURT: No, I read that. And I think it should say that the prospective -- the current and prospective defendants in that litigation disagree with this assessment and the ultimate result is unknowable at this time.

MR. ANKER: Your Honor, that's fine. I was going to say, I was surprised by all of this because in the disclosure statement, there was nothing of the kind. There was simply a statement that they did an investigation and then they filed suit, and then there was a paragraph setting forth our position.

THE COURT: Okay.

MR. ANKER: And our position, including that many of the claims here are time barred, there are releases.

THE COURT: Right. No, that's fine.

MR. ANKER: Your Honor noted today that many of the creditors, when they were dealing with this Debtor, must have thought the Debtor was solvent because they separate -- dealt with separate Debtors. We also noted there that if you look at the market evidence, including where the market price of the stock was, it was in the billions upon billions of dollars. But that's not for today.

I was going to suggest the following language, but I'm happy to have your language, and I'm happy to take out adjectives if they take out adjectives. I was going to say ESL thinks the claims are entirely meritless, and we think the Debtors will receive recoveries of nothing because that is what we think.

THE COURT: All right.

MR. ANKER: But either way, I'm happy to have it. The only other point I would add, Your Honor, and I leave this to you -- I have two other points. One is this is coming under the imprimatur of a court notice, and I think they were emboldened, frankly, by some of what occurred last Thursday.

I think it would be appropriate to add a sentence

that simply says, the Court has obviously not heard any legal argument or heard any evidence and it's not endorsing anyone's view with respect to the litigation.

THE COURT: This is -- I think it just can say there can be no assurance of any recovery.

MR. ANKER: Okay. Your Honor, the last comment I make, and this, I really rise only as an Officer of the Court. It's not -- frankly, if this were true, it might be good for us. There's a paragraph on D&O insurance that says, and the key language here is in bold and italics: "There is at least 150 million of available directors and liability insurance that provides a source of recovery to the Debtor plaintiffs in the subcommittee adversary complaint against various parties."

With that were the case, and maybe it will be. Let me tell you the facts as I interpret them, and you can decide what disclosure you think is appropriate. It is true that the annual policy limit -- so for the 2015 year, separately for 2016, separately for 2017 -- is 150 million. But first, defense costs go against it. And there is, right now, litigation pending, both in state court in Illinois and state court in New York, involving disputes between insurers that D&Os are now being caught in. One litigation, D&Os have commenced, one has been commenced by the insurers, in which they point to different years. One, the primary

insurance, Excel with respect to 2015 says, we are exhausted.

Because one of the things you will hear when you get into this litigation is there was a settlement of litigation relating to Seritage with full releases granted, you'll have to assess the effect of those releases. But it says it is already between that and the Sears Canada litigation fully paid $15 million, so that policy is drawing down to 135 million, and it says that is the only policy that could conceivably bill a year that could conceivably respond.

So if that's right, we're down to 135 million right now, and defense costs are going every day against it. And at the end of the day when the Debtor has a war chest of 25 million for itself alone and there's not just ESL, but lots and lots of different defendants here, they will go through that D&O insurance, at least a good amount of it, I suspect.

Another insurer says, oh no, no, it isn't the 2015 policy -- because they're the second in line, this is QBE -- it is the 2018 current policy, '17 policy -- '18 policy, excuse me, that applies; that's the one that's triggered. Not surprisingly, QBE is not in that, but Excel is; it would have the first 15.

So here's the real truth. There may be 150

million in insurance, minus defense costs; there may be 135 million, minus defense costs. Maybe we can say that some claims are covered by 2018, some are covered by 2015. But one thing is for sure: the insurers are fighting right now paying anything.

THE COURT: Well, that's the case --

MR. ANKER: And so, this disclosure --

THE COURT: -- with any insurance policy, frankly.

MR. ANKER: Your Honor, that's right, that's exactly right. But this is a disclosure to foreign --

THE COURT: No, that's fair. No, I agree with that.

MR. ANKER: This is completely --

THE COURT: So I think you should tone down that description and refer to insurers disclaiming certain coverage.

MR. ANKER: And I would be happy to work with Mr. Singh or others for a disclosure that is accurate.

THE COURT: Okay.

MR. ANKER: But this is simply overstated. And I rose just for those two reasons for disclosure.

THE COURT: Well, I don't know. I mean, having dealt with insurers for too long, it's always good to remind them of the risks of improperly disclaiming coverage too.

MR. ANKER: Understood, Your Honor. Thank you.

THE COURT: Okay.

MR. DUBLIN: Your Honor, Phil Dublin for the record for the Committee. We've done analysis on the Committee's side. We actually believe there may be more than $150 million in insurance.

THE COURT: That's fine.

MR. DUBLIN: I just wanted to clarify Mr. Anker's comments.

THE COURT: I think dollars to doughnuts, some insurer is going to take a different position.

MR. DUBLIN: Oh, I'm sure about that.

MR. ANKER: We too think there may be more insurance.

THE COURT: Right, okay.

MR. ANKER: The (indiscernible) of statement there is.

THE COURT: No, that's fair. You don't want to just fix the amount. I think you need to say that certain insurers have disclaimed some portion of the coverage. And I wouldn't say in excess; I would just say approximately.

MR. ANKER: And we understand that a sentence will be added, Your Honor, in light of your prior remarks that ESL --

THE COURT: Right, strongly disputes all of the claims and there's no assurance of any recovery.

MR. SINGH: That's fair.

MR. ANKER: We'll go with your language.

MR. SINGH: That's fine.

THE COURT: Okay. All right.

MR. FOX: Your Honor, if I may?

THE COURT: Yes.

MR. FOX: Just two points with respect to the order. Edward Fox, Wilmington Trust. First, the paragraph 8 in the proposed order, it's not clear whether the Debtors are saying that the compromises in settlements are effective immediately, meaning now, or immediately upon the effective date. In other language, in other paragraphs, it means on the effective date. I don't know what the intention was here.

The second point, because we're getting a little bit pregnant, so it's helpful to know what and when.

MR. SINGH: Your Honor, I apologize. We can clarify this. It's supposed to be on the effective date, with the exception, I would say, obviously of the administrative expense consent program, which is happening now.

THE COURT: Well, it says they're approved, and then it says will be effective immediately on all parties-in-interest on the effective date.

MR. FOX: It's a little ambiguous. It was

ambiguous to me as to whether effective immediately, stop there, or it was then modified by on the effective date.

THE COURT: I think effecting and binding are the same thing.

MR. SINGH: Right.

MR. FOX: Well, binding -- okay.

MR. SINGH: It's an important -- we'll add --

THE COURT: Well, you can put on the effective date in front, and on the effective date will be effective and binding immediately.

MR. FOX: That'd be fine.

MR. SINGH: Right. And with the exception, of course, of the administrative program.

THE COURT: Right, of the administrative claims.

MR. SINGH: Right.

MR. FOX: And then the other point, Your Honor, I just wanted to clarify in your ruling with respect to the indentured trustees fees. In that, the argument was different than the way you phrased it in your decision, which related specifically -- and seemingly only -- to Wilmington Trust. So I just want to make sure it was not your intention to treat us differently than the other indentured trustees are proposed -- were proposed to be treated.

THE COURT: Well, they didn't object.

MR. FOX: No, no, no. Then they'd be treated better than us; that that was the problem, they were being treated differently, meaning better.

THE COURT: All right. I understand that point. That provision should be modified to just provide for the charging lien and the reasonable fees and expenses for routine ordinary course matters, not any litigation either pro or against the plan.

MR. FOX: Thank you, Your Honor.

THE COURT: I mean, the other folks, I'm assuming, didn't incur those costs because they're not here.

MR. FOX: I'm sure that they incurred costs. I mean, several --

THE COURT: But not the litigation costs.

MR. FOX: Two of them were on the Committee, so I'm sure --

THE COURT: No, but that's -- but that's -- look, if you're on the Committee, that's routine bankruptcy -- I'm just -- I wanted -- your objection really went to, there shouldn't be a penalty for litigating.

MR. FOX: Right.

THE COURT: But that should cover -- there shouldn't be anything for litigating; that's the way you get rid of the penalty. There's no plus for litigating or negative for litigating. So, for example, if you guys had

stood up and filed a 50-page brief in favor of the plan, that shouldn't get paid for under this provision, nor should the objection get paid for. Everything else that you normally do would get paid for.

MR. FOX: Okay. I think we can make that work.

THE COURT: Okay. Because, again, you didn't want to -- the notion was, this should not be a damper on your litigation rights.

MR. FOX: Yes, that's correct.

THE COURT: Okay.

MR. SARACHEK: Your Honor, Joe Sarachek for me and other 15 trade creditors, trade vendors.

THE COURT: Right.

MR. SARACHEK: And particularly in light of the fact that Mr. Wander, who was shepherding along with me this trade ad hoc trade vendor committee. This -- we filed it last night and delivered to the Court, really in response to a colloquy between you and Mr. Wander about the professional fee carveout. We spent an extensive amount of time over the weekend looking at this issue.

And we think there's a serious issue there as to whether, after February 11th, the professional had the right to a carveout. We think that number amounts to some $50 million, and it's at Docket No. 5332. We would ask -- and the Court indicated at the hearing on Thursday that you were

prepared to sit down with the parties and -- I don't know if you used the word mediate, but you certainly spoke to Mr. Wander. And, again, Mr. -- there's probably 50 to 60 members of this ad hoc trade vendor committee, as opposed to trade claims purchasers who have settled to date.

So this is a serious issue. It goes to good faith. We spent a considerable amount of time looking at it. And to the extent that the report -- well, over the week --

THE COURT: I mean, not by the objection deadline, although others raised the objection.

MR. SARACHEK: But what I'd ask, Your Honor, is we see the train is going down the tracks. But whatever the confirmation order might say, to the extent that this issue can be tabled and determined later, it's a significant issue, Judge. It's a significant amount of money. There's a real -- there's a legitimate question in the documents. In fact, there was no budget after February 11th. There was no budget after February 11th that was approved by any other party. Prior to that date, of course, there was a secured creditor.

And so, we would ask that this issue -- and I get it, the hour is late, but this is a significant amount of money. And just to give you a sense on 180 million of administrative claims, this would amount to 25 cents if

those claims were allowed in full.

THE COURT: Well, what you're asking is the same thing Mr. Wander was asking, which I told him last Friday was unrealistic given the parties' rights under the DIP agreement. That being said, I do believe that there should be -- and that this should be put in a notice -- some additional forbearance on immediate payment by the professionals in the case. But it's nowhere close to what you've suggested, which is everything. And that would be part of my ruling.

MR. SARACHEK: Okay. Thank you, Your Honor.

THE COURT: Okay. Frankly, I think it would go to just align the administrative creditors better. I'm sure that will not necessarily endear me to your partners, but --

MR. SCHROCK: Yeah. I mean, Your Honor, may I be heard on the issue?

THE COURT: Sure.

MR. SCHROCK: Okay. It's certainly, you know, this is obv- -- it's an important issue to the professionals. We -- and when we came into these cases, we, you know, on behalf of our partners and our law firms, you know, and consistent with the requirements in the Code, we said we will do so, we'll perform these services provided that we have the protection of this carveout. And that's the basis upon which, you know, we went to, you know, our

firms and did that; as opposed to, when you talk about fairness, an administrative expense creditor extending unsecured credit to Sears, we certainly -- we look at the order, we think it's plain on its face.

This is the specific circumstance in which we have negotiated for this protection. And because we went, and we had made, frankly, another concession that we didn't even think we were required to make, to try and solve an administrative expense creditor objection. I feel like, you know, now we're being thrown in with all other admin claims and the carveout for which we negotiated, Your Honor, is, you know, effectively going to be put on hold.

And I just want to say for the record, you know, listen, we stand by our disclosure, we stand by what we've done in the case. There's been billions of dollars of administrative claims paid in these cases. And now, for some reason, you know, the 150 that's being paid to the professionals are being singled out and parties are plucking at those. And I --

THE COURT: I'm focusing at -- I'm focusing on the -- a portion of the 50 that's currently being held, which I think mostly came in after the sale.

MR. SCHROCK: It did, Your Honor.

THE COURT: Right. And I think a portion of that should -- the collection, their portion of that should be

deferred.

MR. SCHROCK: Your Honor, I don't have a lot of success changing your mind on these sorts of issues. But I will say that when you're talking about --

THE COURT: I'll put it in this context. It's really the same context that Judge Sontchi dealt with in Molycorp. I understand there are carveouts and there are provisions in DIP orders that provide how money is to be spent on professional fees. But there's a separate requirement under the plan that the plan be feasible.

MR. SCHROCK: Certainly.

THE COURT: And while I generally believe that the projections that the Debtors have provided are reasonable under the circumstances. There's $100 million swing even in those projections -- I'm sorry, not 100 million -- a $65 million swing even in those projections of an administrative shortfall. And if you get beyond those -- and my view is the higher end was probably another 10 or million above that. I kept saying I think that the high end was 70 million more, and I think you guys are at 65, 55, that range. The emergent state is going to be considerably delayed because you're not just dealing with preference claims and liquidating the dogs and cats, which are well in the process of being liquidated.

MR. SCHROCK: Right. Well, you know, there is --

there's still an interim comp order that's in effect. There are certainly no final fee applications that are in front of the court --

THE COURT: No, I understand.

MR. SCHROCK: -- in front of the court.

THE COURT: I understand. And that's -- I mean, that's another point I would make.

MR. SCHROCK: Thank --

THE COURT: Which is --

MR. SCHROCK: You know, if --

THE COURT: -- if I'm going to have a holdback, I can do it now or I can do it later. I think it probably makes sense to do it now as part of a finding on feasibility. I mean, I'm just going to the chart here, if I can. The shortfall, as projected, ranges from 36.5 million to 104.5 million. So I can see, even with the claims settlement, that that goes up another, you know, $7- to $10 million.

And more importantly, the low hanging fruit on the preference claims is probably in that 36 to 50 million range. And I think it would be a good thing for this company to go effective at that point, rather than having to win bigger preference claims. Now, that's the legal analysis. Because it's a feasibility analysis, there is a related appearance analysis, which may not a whole lot,

except for the fact that -- whereas, I think it's really a disserve to the professionals to say they've been paid -- they shouldn't have been paid $150 million because they actually really helped bring about the recovery that exists here.

But we're not there yet, we're not at the end game yet, and I would probably, in your next fee application, probably have a callback in light of that. My inclination is to combine both of them now and have a $10 million holdback.

MR. SCHROCK: And, Your Honor --

THE COURT: Actually, 9 million because 1 million was added in. And I think that is approximately on the 50 percent, at least puts at risk kind of the same amount that the claim program puts at risk on the 50 million. I think up until the closing date, and some period thereafter, there's absolutely no question.

And although there's not a lot of case law on this, I think the US Flow case, In re. US Flow Corp., 332 B.R. 792 (Bankr. W.D. Mich. 2005) basically. I think that money is gone, as far as other creditors are concerned. It's not property of the estate, it's gone, there's a true carveout, et cetera. I think once the debt was paid down, I know there's the desegregated account in trust, et cetera, but you still have to go effective. And I think, for me to

make my feasibility finding, that's -- that's called for.

MR. SCHROCK: And, Your Honor, listen, you're the Judge obviously. We want the plan confirmed. And if Your Honor determines that a holdback of $10 million is appropriate from the carveout account --

THE COURT: Well, a total amount, because you probably contributed 3, would be another 9.

MR. SCHROCK: Right.

THE COURT: And it's from the carveout account, which is, you know, all the professionals.

MR. SCHROCK: Yes.

THE COURT: I guess that would be done pro rata.

MR. SCHROCK: And, Your Honor, I think obviously that's fair. But what I don't want to have happen is, listen, my firm --

THE COURT: And have that keep happening? No.

MR. SCHROCK: We need a finding that the order is final.

THE COURT: That's the legal -- that's the legal context; it's to find feasibility.

MR. SCHROCK: Right.

THE COURT: And a reasonable time for the effective date to occur.

MR. SCHROCK: Right. But to continue that -- you know, while we're still performing services --

THE COURT: No, no.

MR. SCHROCK: -- and parties are still challenging a DIP order from --

THE COURT: I'm frontloading --

MR. SCHROCK: -- a year ago?

THE COURT: I'm frontloading the ruling in the context of a feasibility ruling.

MR. SCHROCK: Okay.

THE COURT: Not in the context of unfairness or Rule 60; that's not going to fly.

MR. SCHROCK: Okay.

THE COURT: But I believe that 50 percent -- I'm sorry, the 50 million that's sitting in that account today, this amount should be held back. The fee order still operates going forward, et cetera. I would not expect there to be, you know, further holdbacks.

MR. SCHROCK: Okay.

THE COURT: Because this is simply to ensure that you get to the effective date within a reasonable time.

MR. SCHROCK: Thank you, Your Honor.

THE COURT: Okay. Well, I appreciate your saying thank you. It's not an easy give.

MR. SCHROCK: That's all I could think of to say. No, thank you would be -- but we'll take it.

THE COURT: It's, you know, unfortunately, it's a

lot of money, but it's something that I actually see pretty often in cases, smaller cases, and it's to confirm the plan. It's not for general -- it's not a reflection on the work that was done, just as the fact that allowed administrative claims are not getting paid right now is not a reflection that they're not owed their allowed amount.

But I think, given the testimony and my understanding of the timing on realizing remaining assets, I think the ESL litigation will either go quickly or take a long time, and so you'll be the preference litigation. Even though you have, I think, generally realistic estimates between 11 and 23 percent recoveries, the low hanging fruit is probably going to be, you know, about $50 million, and you need that 10 to sort of get there.

MR. SCHROCK: That makes sense, Your Honor, and know the preference firms are preparing to file most of the lawsuits. I think the court staff was in a bit of a state of shock. By the end, there's about 2,000 preference actions that are going to be filed here over the next couple of days.

THE COURT: All right. Okay. I asked on Friday if there were any other objections besides the 1129(a)(9) and (a)(11) objections, and no one spoke up other than the people who are here today and spoke up today.

In my review of the objections, there were a

couple that I don't think the Debtors' counsel told me were resolved when we started the hearing on Friday. But it seems to me that, looking through them -- looking through them, a couple might not be either resolved or have raised another issue. And I'm thinking of Santa Rosa Mall, who complains about some -- I didn't really understand the objection -- complained about a settlement and somehow it wasn't properly noticed.

Is anyone on for Santa Rosa Mall? They were the ones that hung up? Oh, the whole line just died? Yeah, you can do that? Thanks.

THE COURT: Okay. This is Judge Drain again. The line -- yes. This is Judge Drain again. When the call-in line died, I was starting to say that when the Debtors recited at the start of the confirmation hearing on Friday the plan objections that had been resolved and withdrawn, it appeared to me that most of the remaining objections dealt with either 1129(a)(9) or 1129(a)(11), which I've addressed. I have addressed the handful of objections that I've addressed today that didn't deal with those issues, and also addressed the U.S. Trustee's objection on Friday.

It appears to me in going through the other objections, there may be some objections by parties that have not been formally settled that do not pertain to the issues that I've already addressed. But I'm not sure, so

I'm going to just go through these quickly. And if you're on the phone, you should speak up to let me know if this is still a live objection that you want to argue.

The first one is the objection of Mario Aliano.

MS. HARRIS: Your Honor, this is Sharon Harris. I'm on the phone on behalf of Mario Aliano.

THE COURT: Yes.

MS. HARRIS: And that's correct that my objection has not been addressed yet. If I could briefly just address the Court?

THE COURT: Okay.

MS. HARRIS: Mr. Aliano has a Class 4 general unsecured claim. And if the plan is confirmed, he would get a pro rata share, although not set forth in Section 4.4. Aliano voted to reject the plan and filed an objection, which is very narrow.

As a really quick background, he's the plaintiff in a civil action that obtained a judgment against Sears. Sears then appealed it, and there's an appeal bond to cover the judgment, plus one year of interest. We agreed to only seek the amount of the appeal bond, and the matter is fully briefed on appeal in the Illinois Appellate Court. And also, we have been working with Sears and Transform on a stipulation whereby Transform would be substituted in as the defendant in the Illinois action in place of Sears.

The issue is, we filed a motion to lift the automatic stay, which was previously presented to the court and continued to October 23rd. And the objection to the Chapter 11 plan is that if the plan is confirmed, then Aliano would only be able to get the pro rata share. And all the stays that are in effect would remain in full force and effect, which would effectively deny our motion to lift the stay without being heard on the merits. Plus, we'd like to make sure that our motion to lift the stay is heard on the merits, and that Aliano's civil action is carved out so the stay is not confirmed for his case.

THE COURT: So can the Debtors confirm that the stay motion will still be considered and that the bond doesn't go away as a result of the plan?

MR. FAIL: Your Honor, Garrett Fail, Weil, Gotshal for the record. The automatic stay will remain in effect, as will parties' ability to seek relief from the stay for cause. And we are working with counsel for Mr. Aliano to try to resolve it by stipulation with all the parties.

THE COURT: And the bond -- the bond will still be outstanding. This bond will still be posted. The confirmation doesn't --

MR. FAIL: The Debtors are taking no steps whatsoever with respect to it, so it'll be outstanding to

the extent it was outstanding.

THE COURT: Right. If there's some resolution among all the parties, then the bond will be involved in that. But the confirmation and effective date of the plan doesn't change the status of the bond.

MR. FAIL: Correct, Your Honor.

THE COURT: Okay. And similarly, it doesn't change the fact that if Mr. Aliano wants to proceed with a lift stay motion, he can do that.

MR. FAIL: Correct, Your Honor. We're hopeful that this'll be resolved. We've worked with Transform and with --

THE COURT: But even if it isn't.

MR. FAIL: Even if it isn't the motion will go forward and we'll deal with it at that point, Your Honor.

THE COURT: All right. So, I mean, I frankly wouldn't -- didn't view the plan as changing those rights. I think the record is clear on that effect. If you want to send language to that effect to Weil, Gotshal, you can do that. But I don't -- I didn't read the plan as somehow causing the bond to disappear or the stay motion to be moot.

MS. HARRIS: Okay. Thank you, Your Honor.

THE COURT: Okay.

MR. FAIL: Thank you, Your Honor.

THE COURT: Alpine Creations, I think is now --

it's clear that they are not a releasing party, and I believe the other objection was an 1129(a)(11) and a (9) objection.

MR. CAVALIERE: Your Honor, Rocco Cavaliere at Tarter Krinsky on behalf of Alpine Creations. I actually just got cutoff for five minutes and I just heard you speaking about my objection. I just signed back on.

THE COURT: Right. I just wanted to -- I just wanted to make sure that this is -- if there's anything left at this point on the objection that I haven't already ruled on or confirmed that the plan addressed?

MR. CAVALIERE: Your Honor, I think we had raised a minor objection with respect to our setoff recoupment, and there's some language that was circulated that is acceptable.

THE COURT: Okay.

MR. CAVALIERE: The only objections that remain are with respect to 1129(a)(9) and (11).

THE COURT: All right. So I've ruled on those, although I may have to fight a little bit at the end. Carl Island -- Ireland. Was that -- were the parties able to resolve that with some adequate protection language?

MR. SINGH: Your Honor, we're working on some language to stipulate to the discussion.

THE COURT: Replacement lien?

MR. SINGH: Yeah, exactly, to provide the replacement lien on all assets. I don't know if they're here, but we've exchanged language and we'll take care of that, Your Honor.

THE COURT: Okay. All right. I think (indiscernible) International was an 1129 objection, (a)(9) and (a)(11), if anyone's on if there's anything else that I'm missing.

PeopleReady wanted clarification that its contract is not deem objected since it's subject to the pending assumption notice. Has that been resolved?

MR. SINGH: Your Honor, that issue I don't think is open. I understand that Transform is negotiating directly with that counterparty.

THE COURT: All right. Well, so -- but as far as you're concerned, is it being deemed rejected under the plan or did you -- since there's a pending notice, I guess it's only when that's withdrawn that it is.

MR. SINGH: Correct. It's on an assumption notice that was proposed to be assumed, so the plan is not impacting the issue.

THE COURT: All right. So if someone -- if someone who's a party, a non-debtor contract party, and there's a pending assumption motion --

MR. SINGH: Right.

THE COURT: -- the plan doesn't reject.

MR. SINGH: Correct.

THE COURT: You would separate reject if their assumption notice is withdrawn.

MR. SINGH: That's correct.

THE COURT: Okay. All right. Santa Rosa Mall. I don't know if you heard me or whether the call conked out. I didn't -- some of the points have been resolved, i.e. Santa Rosa is not a releasing party. And I believe Santa Rosa -- well, I'm not sure if there's anything left, let me just put it that way, given the stipulation of voluntary dismissal of its claims in the adversary proceeding. Is there -- is counsel for Santa Rosa on the phone?

MR. CHICO: Yes, Your Honor. Good afternoon. Gustavo Chico on behalf of Santa Rosa.

THE COURT: Is there anything left to the objection, other than clarification that Santa Rosa is not a releasing party?

MR. CHICO: Right. That's basically what we're trying to get a clarification on that. We were often --

THE COURT: Well, that's clear. The Debtors are treating all parties who objected on the basis of a third-party release, or of course, who opted out, as a non-releasing party.

MR. CHICO: Right. And our concern was regarding

the injunction provision in Section 15.8 of the plan. The way it's drafted, it seems that parties will be -- Santa Rosa or any party will be injuncted from collecting or otherwise recovering by any means or manner, whether directly or indirectly. And since we're trying to pursue our claim against the insurance carriers from the insurance company, that that may be construed as an indirect action against the Debtor, and that's why we wanted that clarification.

THE COURT: All right. Well, I don't read the injunction as protecting third parties.

MR. SINGH: That's right, Your Honor. It's just for implementation of the plan as it relates to the Debtors.

THE COURT: As it relates to the Debtors.

MR. SINGH: Right.

THE COURT: I think maybe the thing to do is simply to send a letter and I'll put it on the docket to Santa Rosa confirming that.

MR. SINGH: Sure, we can do that, Your Honor.

THE COURT: Okay.

MR. CHICO: Thank you.

THE COURT: Okay. Edgewell Personal Care, in addition to the 1129(a)(9) and (11), objected on the basis that it's not clear whether its contract is assumed or rejected, and is arguing that it was a de facto assumption,

which isn't true -- I mean, there's no de facto assumption under the Bankruptcy Code. But can you clarify whether it's being assumed or rejected as of the confirmation date?

MR. SINGH: One second, Your Honor.

THE COURT: Okay.

MR. SINGH: Your Honor, my understanding with respect to this agreement is that it's not an executory --

THE COURT: Not an executory contract.

MR. SINGH: Right, as of today. So I think there may just be a dispute with respect to whether or not we've assumed or rejected it, which may have to happen.

THE COURT: All right. Well, you've done neither, right, at this point?

MR. SINGH: Right, we've done neither; that's exactly right.

THE COURT: So my ruling is, you have to either do -- let me back up. There's no such thing as a de facto assumption or rejection while you're in bankruptcy prior to the confirmation date.

MR. SINGH: Right.

THE COURT: If the plan is confirmed and it goes effective and you've done nothing, the contract, to the extent it's executory, rides through.

MR. SINGH: No, Your Honor. The plan says it's rejected if we've done nothing.

THE COURT: If you've done nothing.

MR. SINGH: Right.

THE COURT: Okay, correct. So if there's not been a notice of assumption, it will be deemed rejected.

MR. SINGH: Correct.

THE COURT: All right.

MR. SINGH: And I guess they can try to argue whatever they want later.

THE COURT: Well, you can't argue that there's a de facto assumption.

MR. SINGH: Right, because that issue, you've ruled on.

THE COURT: Right. See, among other authorities, In re. Child World, Inc., 147 B.R. 847 (Bankr. S.D.N.Y. 1992), but also the plain language of Section 365. So I don't know if Edgewell's counsel is on the phone. But, consequently as a consequence of the plan's confirmation and there being no assumption notice, it's deemed rejected to the extent it is executory.

MR. SINGH: Right.

THE COURT: That's an open issue too, whether it is executory. Vehicle Service Group, in addition to 1129(a)(9) and (a)(11) raise the third-party release point. But the Debtors have confirmed that it is being treated as opting out of the third-party release. Is counsel for VSG

on; is there any other issue that I missed here? Okay.

I think we briefly addressed this, but Team Worldwide Corporation, I think you've resolved it.

MR. SCHROCK: It's resolved, Your Honor, yeah.

THE COURT: Okay. And that's correct, Team Worldwide are you on? No, okay. All right. Is there any objection that I missed? Okay.

Let me go back then to the 1129(a) findings. I'm prepared to make each of the findings that I need to make under 1129(a) for confirmation of the plan. I've already ruled as far as the PBGC classification; that the plan complies with the other provisions of the Bankruptcy Code as far as classification is concerned. With regard to the only objection, I believe that was to classification, which was to the classification of the PBGC claim. There's clearly a reasonable basis for classifying that claim separately, given the PBGC's rights and position in the case.

I also find that the plan is proposed in good faith under 1129(a)(3). It's been proposed for a valid bankruptcy purposes, and I believe is intended to and does have the best chances of maximizing recoveries for creditors here, and has been carefully thought through to do so in a way that is fair in light of all the creditors' rights under the applicable agreements and the Bankruptcy Code, including the DIP agreement and order, the cash collateral order and

the carveout provided for in it, including the language that I've already referenced regarding the placement of the carveout amounts in a segregated account and in trust solely for the use of the professionals.

The only other objections on 1129(a) grounds were on the requirement 1129(a)(9) that to be confirmed, a plan must accept, to the extent of a particular claim has agreed to a different treatment of such claim, provide that, with respect to the claim of a kind specified in Section 507(a)(2) or 507(a)(3) of this title. On the effective date of the plan, the holder of such claim will receive on account of such claim cash equal to the allowed amount of such claim.

1129(a)(11) provides that the plan proponent must show, as it must show with regard to all the 1129(a) provisions by a preponderance of the evidence that, quote, "Confirmation of the plan is not likely to be filed by the liquidation or the need for further financial reorganization of the Debtor or any successor to the Debtor under the plan, unless such liquidation or reorganization is proposed in the plan.

I'll note that Section 1129(a)(9) does not require that confirmation of the plan be immediately followed by the effective date of the plan. It simply requires that on the effective date of the plan, the plan provides for payment in

cash of the allowed amount of administrative expenses, with the exception of those where the holder has agreed to a different treatment of such claim.

Here, as with many plans, the Debtor has proposed -- the Debtors are proposing that the Court confirm the plan, knowing that there will be a hiatus while the Debtor is still a debtor-in-possession until the plan goes effective. That is because there is a projected shortfall, as of today, of between $36.5 and $104.5 million of cash payments necessary to implement the plan, including payment of projected allowed administrative expenses -- priority tax, secured claims, and priority non-tax claims -- in light of the Debtors' projection of sources beyond those that are in hand.

Having reviewed the Declarations, including the supplemental Griffith Declaration in support of confirmation of the plan, I find that the witnesses testimony, including on cross-examination, is credible and that the projections are reasonable. Nevertheless, they are just projections and, as I said, they show a shortfall of between $36.5 and $104.5 million if the plan were to go effective promptly upon entry of the confirmation order, i.e. later this week, for example.

Based on the total sources, however, I believe that it is reasonable to project substantial recoveries in a

relatively brief period on the Debtors' preference claims and/or settlements of administrative expenses that would include a preference claim release in return for a reduction of the administrative claim. That would reduce that shortfall dramatically.

I also believe, based on Mr. Transier's Declaration, which was uncontroverted in my own review of the Complaint attached to it, that the Debtors have substantial potential claims against the defendants in that adversary proceeding, which clearly will take longer to test and potentially obtain recoveries on, but -- which have been treated throughout these cases by the Debtors and the Creditors' Committee, both represented by well-informed and sophisticated counsel, as claims that should not be settled for relatively small amounts.

However, that litigation, I believe, unless there is a meaningful settlement of it in the relatively near term, I think will take a substantial amount of time to resolve, potentially two to four years, and I am reluctant to delay the effective date of this plan that long.

So I am focused on the claims' side of the balance sheet, the administrative claims' side of the balance sheet and the other 100-cent dollar amounts that would need to be paid, as well as the other assets besides the so-called ESL litigation. Based on the record before me and including the

additional exception from the carveout that I've previously discussed on the record of another $9 million, I believe that the likelihood of satisfying Section 1129(a)(9) in the relatively near term, i.e. in a matter of a few months, is established.

I have additional comfort, besides the concession I've asked of the professional here, in that conclusion from the claims' resolution program that I am also approving today and then would become effective today, which would provide for incentives to settle claims for less than 100 cents on the dollar by administrative expense creditors.

It has been argued that that settlement has been announced too promptly for proper review. And, secondly, that the, in essence, third tier of the settlement or sandwich group in the settlement who neither affirmatively opt out or opt in, are not really -- or I couldn't find would be really agreeing, for purposes of 1129(a)(9), to their treatment under the settlement.

As to the first point, I do not believe that the settlement requires more notice to parties-in-interest generally. I say so because it appears to me to be a reasonable resolution of a relatively simple issue, which is that the Debtors lack sufficient cash to pay administrative expense claims in full, but have agreed on a reasonable mechanism supported by informed counsel on both sides -- and

that includes the Official Unsecured Creditors Committee -- as to the allocation of a meaningful amount of cash in return for a discount for opting in to the settlement and a second tier of meaningful cash, albeit it a later tier, for doing nothing and obtaining a 5 percent greater maximum recovery, as well as the option clearly to opt out and simply wait for a full 100 percent recovery.

Given those options for administrative expense creditors, I don't believe any administrative expense creditor can criticize the settlement. They have the option either to be bound by it or not be bound by it. And, therefore, it's neither too good nor too poor, because both options are available to them under it. And I believe now, they have more than sufficient time to review it to make that choice, i.e. the 33 days plus the disclosure, as modified on the record today, of the risk factors.

The second objection, as I noted, is that I should not find that parties who neither affirmatively opt in nor affirmatively opt out can be said to have agreed to the settlements' treatment of that group for purposes of Section 1129(a)(9). The agreement here is not the deemed agreement that I've consistently found is proper to find, if there's proper disclosure, under a plan, which has its own specific treatment under Section 1141 of the Bankruptcy Code, i.e. it's binding, the terms of the plan are binding on all

parties.

The agreement here is an agreement under normal contract law principles. So the issue for me is can one agree under normal contract law principles by implication or non-action. This issue was dealt with by Bankruptcy Judge Bernstein in In re. Teligent, Inc., 282 B.R. 765 (Bankr. S.D.N.Y. 2002), where he determined under those circumstances that administrative expense creditors who did not return a consent form would be deemed to agree, inferred to agree, having been given the option to either object or to affirmatively agree.

Judge Bernstein concluded with appropriate disclosure, as there was here in an effort to provide enough notice to parties to make a decision, that he could infer agreement under applicable non-bankruptcy law, including the Restatement (Second) of Contract, Section 69-1, which sets forth exceptions to the rule that ordinarily an offeror cannot treat silence or inaction as an acceptance. The exceptions where the offeree will be deemed to accept the offer through silence are when he has a duty to speak and, second, when the offeree's silence may constitute acceptance where the offeror has stated his intention or given the offeree reason to understand that he will do so, and the offeree, in remaining silent and inactive, intends, therefore, to accept the offer.

That latter principle, I believe, applies here, although, frankly, Judge Bernstein applied the former too, finding a duty to speak in the context of plan confirmation where it would be clear to the party that the plan was being confirmed in reliance on that construct, which is clearly the case here because it is part of my 1129(a)(11) analysis that at least some parties will neither opt in nor affirmatively opt out of the settlement.

There's not a lot of case law on this issue, at least one case. In re. Real Wilson Enterprises, (indiscernible) B.R. LEXIS 3997 (Bankr. E.D. Calif. September 23, 2013) has disagreed with Teligent. But I believe it does so under quite different facts where the choice was not laid out in a way that was laid out in Teligent or here. In re. Global Aircraft Solutions, Inc., 2011 B.R. LEXIS 2063 (BAP 9th Circuit, May 11, 2011) relied on the Restatement provision that I previously cited for a deemed consent. And there is precedent from the Toys 'R Us case where a similar program, albeit one without a lengthy opinion, but a bench ruling in favor of the same type of notice and deemed consent.

Given that the Debtors are relying upon a different treatment where there is silence than either of the other two options where there was affirmatively reaction, can that reliance carry through in this case,

including in respective rulings on feasibility. I believe that under these circumstances, I can find agreement under normal contract law principles.

So the only other finding I need to make is against entities that have not objected to confirmation, which is the cramdown finding, for those classes that have not accepted the plan and certain Debtors. It's clear from the plan that no junior class is receiving any property under the plan; and, consequently, the plan satisfies the requirements of the cramdown of the unsecured non-voting classes, as well as the equity classes.

I had I believe already ruled on the other objections by the United States Trustee, and I will not reiterate my ruling here on that, other than to note that for the same reasons that I previously ruled, and certain colleagues of mine have previously ruled. I believe that in connection with the plan with a disclosure statement ballot and plan itself alert creditors that if they do not opt out of a third-party release, they will be bound by that release means that if they do not object to the release, they are bound by the terms of the plan as provided in 11 U.S.C. Section 141 of the Bankruptcy Code, i.e., the plan is more than just a contract by analogy; it has its own statutory and common law res judicata effects, including with respect to any provision, including a release provision, as long as

the release provision is drafted clearly and the option to opt out is clear.

Here, the Debtors have treated not only those who affirmatively opted out, but those who have actually objected to confirmation on the basis of the third-party releases, having opted out of the release. The other parties who have done nothing should be bound by the plan, given the clarity of the release and the fact that it is not unduly broad and, instead, is carefully tailored and has authority for that proposition. I'll simply refer to the Debtors' reply memorandum of law, which cites my prior rulings on that topic, as well as rulings by Judge Lane and Judge Chapman.

So I think you need to make some relatively modest changes to the confirmation order. And you don't need to formally settle those -- that draft, but you should circulate it perhaps a day before the submission of it to chambers.

I guess I should also say, although I said this during oral argument on Friday. Certain objectors have questioned why one should proceed to confirmation now, as opposed to waiting until more cash is brought into the estate. In my view, the Debtors and the Committee are entirely correct in seeking confirmation at this point. It has helped to provide enough certainty and clarity for, at

this point, the administrative expenses creditors primarily to be ready to focus on a resolution of their claims, and has further, I believe, and materially so, reduced the continuing costs of these cases where uncertainty inevitably would lead to more issues to be litigated, raised and disposed of, with an eye to positioning the parties for an ultimate confirmation fight. It's better to have had that fight over the last two days of hearings and be in a position now where the Debtors have a clear path to going effective.

MR. SCHROCK: Thank you. Thank you very much, Your Honor. On behalf of the Debtors and the Board, the restructuring committee, and all the constituents, we really do appreciate it.

I have one last just housekeeping item. It's not a matter for today. But the ad hoc administrative claimants, you know, we've incurred, you know, roughly $700,000 in fees and, you know, getting to the consent program here. The Debtors and the Committee did agree that they would support their motion for substantial contribution up to $400,000. I know that's not up for today, but I did want to note that for the record because it is certainly part of our agreement.

THE COURT: Okay. Well, as we made clear, until the plan goes effective, all of the rules and principles of

an ongoing Chapter 11 case applies, so I'm sure I'll have that application in due course. Okay. All right. Thank you.

MR. SCHROCK: This is Ms. Marcus. If we could just very quickly, I'm sorry.

THE COURT: That's all right.

MS. MARCUS: Sorry. Sorry to keep everybody here any longer. Just very quickly, Your Honor. As you know, we had the 1114 hearing on Thursday.

THE COURT: Right.

MS. MARCUS: Your Honor ruled we submit an order.

THE COURT: Right. I sent an order in to be entered last night.

MS MARCUS: Perfect. We haven't seen it yet.

THE COURT: I read Mr. -- well, I sent in, like, 60 orders over the weekend, so they've been busy. They'll be entering it soon. I read Mr. Gerson's letter, and I had a very minor change to the order in light of the letter, but I didn't redo the settlement. And I think that was the problematic aspect of the letter is there was some aspects of the letter that really sought to redo that settlement, and I wasn't going to do that.

MS. MARCUS: Thank you, Your Honor.

THE COURT: Okay.

(Whereupon these proceedings were concluded at 05:27 PM)

C E R T I F I C A T I O N

I, Sonya Ledanski Hyde, certified that the foregoing transcript is a true and accurate record of the proceedings.

Sonya Landanski Hyde

Digitally signed by Sonya Landanski Hyde
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